

Section 25 Report from Chief Financial Officer

Fiduciary and Statutory Considerations

In setting the budget the Council has a duty to ensure:

- It continues to meet its statutory duties
- Governance processes are robust and support effective decision making
- its Medium-Term Financial Strategy reflects the significant challenges being faced and remains responsive to the uncertainties in the economy by continuing to deliver against its savings targets
- its savings plans are clearly communicated and linked to specific policy decisions, with the impact on service provision clearly articulated
- It understands profile of existing and forecast liabilities and makes sufficient provision for repayment
- it has the appropriate levels of reserves and that it closely monitors its liquidity to underpin its financial resilience
- it continues to provide support to members and officers responsible for managing budgets
- it prepares its annual statement of accounts in an accurate and timely manner

In making decisions in relation to the revenue budget and council tax the Council has various legal and fiduciary duties. The Council is required by the Local Government Finance Act 1992 to make specific estimates of gross revenue expenditure and anticipated income leading to the calculation of the council tax requirement and the setting of the overall budget and council tax. The amount of the council tax requirement must be sufficient to meet the Council's legal and financial commitments, ensure the proper discharge of its statutory duties and lead to a balanced budget.

In exercising its fiduciary duty, the Council should be satisfied that the proposals put forward are a prudent use of the Authority's resources in both the short and long term; that the proposals strike a fair balance between the interests of Council taxpayers and ratepayers, current and future, on the one hand and the community's interests in adequate and efficient services on the other; and that they are acting in good faith for the benefit of the community whilst complying with all statutory duties. Officers have addressed the duty to strike a fair balance between the different elements of the community and the interests of council tax and business rate payers in developing the proposals which are set by reference to the strategic outcome priorities in the Working for All Strategy.

Section 25 of the Local Government Act 2003 requires the Finance Director to report to the Council when setting its council tax on:

- the robustness of the estimates included in the budget, and
- the adequacy of the financial reserves in the budget.

The Council is required to have regard to this report in approving the budget and council tax. The Finance Director has reported on the Medium-Term Financial Strategy to the Executive through 2022/23, the last update report was to the 19th January meeting. This report is now going to the Council to make its final decision.

Section 25 concentrates primarily on the risk, uncertainty and robustness of the budget for the next financial year rather than the greater uncertainties in future years. Given the significance of the funding reductions over recent years and the impact that the changes in behaviours since the pandemic is having on the Councils' investments into regeneration and

returns from its commercial estate, this report considers not only the short-term position but also the position beyond 2023/24 in the context of the Council's current Medium Term Financial Strategy (MTFS).

Section 28 of the Local Government Act 2003 also imposes a statutory duty on the Council to monitor during the financial year its expenditure and income against the budget calculations. If the monitoring establishes that the budgetary situation has deteriorated, the Council must take such action as it considers necessary to deal with the situation. This might include, for instance, action to reduce spending in the rest of the year, or to increase income, or to finance the shortfall from reserves.

Section 114

Under Section 114 of the Local Government Finance Act 1988, where it appears to the Finance Director that the expenditure of the authority incurred (including expenditure it proposes to incur) in a financial year is likely to exceed the resources (including sums borrowed) available to it to meet that expenditure, the Finance Director has a duty to make a report to the Council.

The report must be sent to the Council's External Auditor and every member of the Council and the Council must consider the report within 21 days at a meeting where it must decide whether it agrees or disagrees with the views contained in the report and what action (if any) it proposes to take in consequence of it. In the intervening period between the sending of the report and the meeting which considers it, the authority is prohibited from entering into any new agreement which may involve the incurring of expenditure (at any time) by the authority, except in certain limited circumstances where expenditure can be authorised by the Finance Director. Failure to take appropriate action in response to such a report may lead to the intervention of the Council's Auditor.

Section 25 Summary Overview

The Council is able to set a balanced budget for 2023/24 with the use of £8.3m one off reserves and has made arrangements:

- To operate a cost control framework and discipline
- To establish further savings over the MTFS period through developing a minimum viable position for all services
- To comprehensively track savings and establish full financial variance monitoring in a timely way
- For a Fit for the Future programme that has to balance implementing a strong programme discipline for delivery critical savings plans alongside establishing the future state of the Council.
- For reviewing the prudent position on the amounts set aside for debt
- To stabilise reserves
- To review Company business plans and investments

It is not evident at this stage, however, how the Council will establish a balanced budget for 2024/25 and the MTFS period. The Council is in the territory of S114 but as of the date of this report a S114 Notice is not required. This report however may lead to the issuing of a S114 Notice in 2023/24 as work on the 2024/25 budget progresses.

There are sections in this report that are made in bold for attention. This summary overview section extracts these for ease of reference.

The Council does need to make significant improvements in its approach to resource management as a strategy and discipline

The requirement to make savings has dominated the budget setting process in 2021/22 and 2022/23 and this will be an even more dominant feature for the 2023/24 – 2025/26 MTFS period and the foreseeable future beyond this term. The 2023/24 budget is only balanced with the use of £8.3m reserves and it will take a significant re-think and restructure of the Council, its investments and strategic partnerships in order to deliver an operational reset.

The Council has a significant dependency on the income generated from its commercial estate. All of this income is taken directly to the general fund and the Council will need to develop an approach to smoothing this reliance on income over a longer trading period.

The Council has some exposures which are more significant than other local authorities:

- The level of dependency on combined income from the Council's off-street car parking and commercial estate which is disproportionate to the Council's financial resilience and ability to respond to such an economic downturn.**
- The size of borrowing alongside the policy it has adopted on Minimum Revenue Provision is equally disproportionate to the Council's financial size, resilience and ability to respond to risks in the event of needing to impair loans**

The costs and lost income experienced over the last 2 years, and the financial climate post pandemic, have resulted in the financial position now becoming an immediate problem.

The Council does not have the financial resilience to absorb the impacts of the current economic downturn and changes in consumer behaviours in the short and medium-term and cannot solely rely on its investment approach to protecting services. The Council needs to develop a more far-reaching strategy of service transformation that will enable it to manage within the predicted level of funding available whilst both ensuring it maintains the services it is statutorily required to provide and uses the strategic priorities established within the Woking for All strategy to target funding.

The Council has not undertaken a review of its compliance with this CIPFA Financial Management Code as of the date of this report. The Council will need to programme in a review in 2023/24 as part of its delivery of the MTFS strategy.

Audit Opinion on the Council's Accounts

The Council does not have an audit opinion on its accounts for 2019/20 and subsequent years (2020/21 and 2021/22). This position creates a significant risk for the Council as it cannot place any reliance on prior year accounts.

The Council has raised its concerns with its auditors and has engaged with the Financial Reporting Council (FRC) and Public Sector Audit Appointments (PSAA). The Council recognises that the delay in audits is a national issue for the sector, however, it has been seeking what options are available to specifically respond to the situation and delays in Woking Borough Council.

The delay to the Council's accounts relates to the consolidation of group companies into the Council's accounts. An outline timetable of this work has been discussed with the Council's auditors to progress this work for completion by September 2023. This is however subject to risks around resourcing this work by the auditors, the Council's finance team and the Group Companies finance teams. By September 2023 there will be a 3 year delay of external audit.

At this stage the Council are not able to get any feedback from its auditors on its 2020/21 and 2021/22 accounts in advance of getting an audit opinion on the 2019/20 accounts. The Council will continue to engage with the FRC and PSAA where this can assist the Council to address the delays in its external audits and where it can assist the sector to address the backlog in audit opinions on accounts.

Robustness of Estimates in the Budget

The budget setting process within the Council has been operating effectively for many years but has been placed under significant strain over the 2021/2 and 2022/23 years arising from three predominant factors:

- The previously adopted approach the Council had taken to invest in the Woking economy and Council assets as a way of generating income that counteracted budget pressures was no longer a sole viable strategy
- The council had relatively little experience of delivering notable service and budget reductions, nor does it have the capacity for delivering a savings based approach to addressing a significant budget shortfall
- The impact of the Covid-19 pandemic and subsequent downturn in the economy was disproportionate to the Council's financial resilience and its ability to manage the impacts, particularly in the short term.

The underlying assumptions within the MTFs are continually reviewed to provide the most reliable projection of the future financial position. In many cases this will result in a range of potential scenarios for consideration.

The implications of these factors are that the Council does need to make significant improvements in its approach to resource management as a strategy and discipline, specifically in relation to:

- Producing comprehensive in-year full financial variance monitoring in a timely way
- Aligning financial reporting to the new organisational structure of the Council and budget holding responsibilities

- Thorough and systematic tracking actual savings delivered against savings decisions and financial planning assumptions
- Targeting financial performance reporting on the key areas of financial risk and volatility
- Developing a stronger strategic commercial oversight of the Council's investment in its wholly owned and joint venture companies

A new performance reporting framework has been proposed and agreed in 2022/23 which replaces the Green Book reporting. This needs to be adopted as soon as possible in 2023/24.

The requirement to make savings has dominated the budget setting process in 2021/22 and 2022/23 and this will be an even more dominant feature for the 2023/24 – 2025/26 MTF period and the foreseeable future beyond this term. The 2023/24 budget is only balanced with the use of £8.3m reserves and it will take a significant re-think and restructure of the Council, its investments and strategic partnerships in order to deliver an operational reset.

A major transformation programme, Fit for the Future, is being put in place to effectively and corporately design and deliver this reset and manage the delivery of savings within the required timescales, or as is more recently the case, to provide cash flow funding to support a longer delivery timescale for the more complex elements of the Programme. This is an emerging programme and therefore has to balance implementing a strong programme discipline to critical savings plans and cost control measures, alongside establishing what the future state of the Council needs to be.

The flexible use of capital receipts for the Fit for the Future, as an invest to save, to generate savings through a fundamental reset of how the Council operates will be essential and is being reported in the MTF report to the 23 March 2023 meeting of the Executive and for approval at 30 March 2023 meeting of Council.

More detailed financial and performance modelling is being developed for the Council's commercial estate, drawing from national forecasts in respect of performance of retail and office sector assets. **The Council has a significant dependency on the income generated from its commercial and off street car park estate. All of this income is taken directly to the general fund and the Council will need to develop an approach to smoothing this reliance on income over a longer trading period.** The shortfall of forecasted income against budgeted income is c£5.5m (c18%) per annum in the short term, 1-2 years. Whilst this is reflective of the national picture in respect of these commercial assets, and Woking is out-performing the national position in some areas, it does represent a variance that the Council does not currently have the financial resilience to be able to manage.

Budget management within the Council requires strengthening which is supported by the actions that have been taken to strengthen financial variance reporting and savings tracking.

Risk and Financial Resilience

The Council has a Risk Management Strategy that is reviewed annually. Within the strategy the Council has a Strategic Risk Register that is held by the Council's Corporate Leadership

Team. The Strategic Risk Register is being reported to the Executive and is reviewed by the Overview and Scrutiny Committee

As can be seen from the Strategic Risk Register, the risk of not being able to set a balanced budget has been identified as the most significant risk to the Council (risk 1 in the strategic risk register). Despite the mitigations highlighted in the register the level of risk remains outside of the Council's established risk appetite and therefore further mitigating actions have been initiated, targeted at bringing the risk towards a level that the Council can tolerate.

It has been recognised, in updates to the MTFs over the last 2 years, from the outset of the Covid pandemic, that the financial position of the Council was in a critical position. The Council had been able to maintain services and provide community infrastructure as a result of its strategy to develop alternative sources of funding through investing in local assets that provide a commercial return for the Council. These returns are then invested in delivering services to the communities of Woking.

The pandemic resulted in an immediate, and dramatic, fall in activity and footfall severely impacting the Council's car parking revenue and affecting tenants across all of the commercial estate. It has become clear over the last 10 months that, despite the removal of all Covid restrictions, the economic model on which the Council's budget is based has changed. The Council made an application to Government in 2021 for exceptional support. This application was due to the impact the Covid 19 pandemic had on its commercial income budgets.

The basis of the application related to the impact that Covid 19 was having on the economy and specifically the reduction in income to the Council from car parks and its commercial estate. The Council maintained, at the time, that it had the financial strategy to withstand the vagaries of normal economic cycles but Covid impacts far exceeded the scenarios it envisaged and therefore the Council sought support to enable it to capitalise its "losses" so that these could be spread over time.

The application for Exceptional Support was not approved. It was recognised that although some elements of the financial position in the Council are exceptional, it did not have an immediate and pressing problem in its finances, rather it predicts that it may run out of resources in the medium term.

Many other Councils are experiencing financial pressures from both the current high levels of inflation and the ongoing impact of the pandemic, Brexit and the war in Ukraine. In recent months increasing numbers within the sector have expressed concerns about the sustainability of budgets and ability to balance finances in the current economic climate. The challenge of inflationary pressures on services being experienced by the Council is one shared across the sector. **This Council has, however, some exposures which are more significant than other local authorities:**

- **The level of dependency on combined income from the Council's off-street car parking and commercial estate which is disproportionate to the Council's financial resilience and ability to respond to such an economic downturn.**
- **The size of borrowing alongside the policy it has adopted on Minimum Revenue Provision is equally disproportionate to the Council's financial size, resilience and ability to respond to risks in the event of needing to impair loans**

The costs and lost income experienced over the last 2 years, and the financial climate post pandemic, have resulted in the financial position now becoming an immediate problem.

The July MTFS report provided an update on the development of the Council's Financial Resilience Strategy, a key component of the Council's MTFS. A full overview on all of the actions taken on the Financial Resilience Framework will be included in the MTFS update report to the 23rd March 2023 meeting of the Executive and 30th March meeting of Council. This overview forms an integral part of the S151 Officers view on their statement of budget robustness and sustainability.

The Council does not have the financial resilience to absorb the impacts of the current economic downturn and changes in consumer behaviours in the short and medium-term and cannot solely rely on its investment approach to protecting services. The Council needs to develop a more far-reaching strategy of service transformation that will enable it to manage within the predicted level of funding available whilst both ensuring it maintains the services it is statutorily required to provide and uses the strategic priorities established within the Woking for All strategy to target funding.

The Adequacy of Reserves

The Council has a risk-based reserves strategy and policy on general balances. The prudent level established is £10m which reflects 10% of operational expenditure (£5m) plus £5m for business change and budget savings risk. Whilst this level of general reserve is high for a District Council it is representative of the financial risks facing the Council and remains appropriate.

The Council has historically held a series of earmarked reserves with funds set aside to address specific risks to the Council's financial position. Since 2020/21 significant reserves have been used to support the Council's service provision following reductions in income and increasing costs. Operational deficits in 2020/21, 2021/22 and forecast for 2022/23 have substantially reduced the buffer previously provided by reserves which had been accumulated over time to mitigate annual revenue fluctuations, cyclical economic cycles and one-off project and transformation costs.

Ongoing forecast deficits reported through the MTFS result in a continued use of reserves to support the in-year budget position. All funds which can be used, including those previously earmarked in individual reserves and the General Fund balance, are now considered in aggregate as available resources to allow time for costs to be brought in line with income. Despite this, without action to reduce deficits, balances will fall below the minimum level during 2024/25 and be fully utilised during 2025/26.

A fundamental reduction in the net cost of services provided is required immediately before the reserves are fully utilised.

Introduction of Cost Controls

There is a need to further strengthen the controls that are in place over spend in order to respond to the projected budget gap in this year of £8.8m, which will continue to be a gap

of £8.3m in 2023/24. The Council must take all arrangements to bring spending back in line with the budgets we have available, in the short and medium term.

Councils are required by law to have balanced budgets. If a council cannot find a way to finance their budget then a Section 114 (S114) must be issued. The issuing of a S114 notice bans all new spending with the exception of protecting vulnerable people and statutory services and pre-existing commitments.

The Council is in the territory of S114 but as of the date of this report a S114 Notice is not required The criteria however is being used to help steer the Council's control of spend. A number of steps are being taken to bring planned spend down to within the level of funding available and as part of these measures, the Council has moved to essential spend only. Any spend that is discretionary and can be avoided or deferred should not be made. The criteria for essential spend is:

- Existing staff payroll and pension costs
- Expenditure on goods and services which have already been received
- Expenditure required to deliver the Council's provision of statutory services at a minimum possible level – we call this the minimum viable position
- Expenditure within HRA to meet regulatory standards
- Urgent expenditure to safeguard vulnerable residents
- Urgent expenditure in response to issues of health and safety in council buildings and in areas of public realm
- Expenditure required through existing legal agreements and contracts
- Expenditure required through ring-fenced grants or third party funding
- Expenditure necessary to achieve value for money and/or mitigate additional in year costs
- Expenditure to deliver future savings

These spend control measures have been formally established and will remain in place until the Chief Executive alongside the Finance Director (S151 officer) determine they can be released. This assessment will be subject to review through the established MTFs.

In addition to control over the Council's direct expenditure, there has also been increased scrutiny and challenge of the Thamesway Group business plans for 2023. These plans were due to be approved in December 2022 however, as set out in an update to the December meeting of the Executive, the Council's Shareholder Advisory Group (SAG) has requested further exploration of a number of options that would have the impact of reducing the Council's Capital Finance Requirement; minimising risk associated with loan exposure and improve the controls the Council applies to the release of further loan funding.

Updated plans have been further reviewed by the SAG, and the Thamesway Board, and are being brought forward for approval to the 23rd February 2023 meeting of Council

Minimum Revenue Provision

The Council has very high levels of borrowing. The current policy and judgement in assessing the appropriate level of Minimum Revenue Provision (MRP), the amounts set aside for the repayment of that debt, enables a balanced budget to be set. There is a significant and substantial risk that a more prudent assessment of MRP provision should be adopted. At this stage no additional prudent provision has been made and any change in assessment of MRP would result in an unsustainable position.

There is equally a significant and substantial risk that a more prudent provision for impairment of capital loans should be made. At this stage no additional prudent provision has been made and any change in assessment of MRP would result in an unsustainable position.

If it is assessed that there is a risk of impairment of capital loans then it is appropriate to commence charging a MRP on the balance. The review of both Thameswey and Victoria Square investments indicate risks through asset values less than loan balances, reductions in valuations, long term business plans which are sensitive to assumptions and require support for many years, and losses which may be realised and not contained within the Group.

The government have previously consulted on changes to the guidance for provision of MRP. Given the level of investment the Council has made through capital loans, any changes which affect these loans are likely to cause an additional unsustainable pressure to the General Fund budget.

The Council's position on MRP will be subject to further independent assessment and review. An independent review has been commissioned on the Council's MRP policy, and the amount that has been accounted for in its accounts, to be completed by early April 2023. For this MTFS report the MRP policy adopted in 2022 is being rolled forward and any amendments required following the independent review will be brought forward in 2023/24 as part of the MTFS reporting.

CIPFA Financial Resilience Index

Following the events in Northamptonshire and a heightened national focus on the finances of local government more generally, the Chartered Institute of Public Finance and Accountancy (CIPFA) produced a Financial Resilience Index (FRI). The index uses a range of financial information and other factors to generate a series of measures against which all authorities are 'stress tested', although clearly Covid-19 has created a very real and more complex stress test than we would ever have modelled for.

CIPFA's Financial Resilience Index is a comparative analytical tool that may be used by Chief Financial Officers to support good financial management, providing a common understanding within a council of their financial position. The index shows a council's position on a range of measures associated with financial risk. The selection of indicators has been informed by extensive financial resilience work undertaken by CIPFA, public consultation and technical stakeholder engagement.

The Woking Resilience Index results can be accessed directly from the CIPFA website at [Financial Resilience Index | CIPFA](#). The 2021/22 revenue outturn information remains outstanding and will be returned to Government in April 2023.

As can be seen from the information presented, the analysis indicates areas of lower risk around level and sustainability of reserves and income generated through fees and charges alongside some areas of higher risk around changes in reserves; the level of debt and level of interest payments.

The position on the level and sustainability of reserves has however changed during 2021/22 – 2023/24 and this is now a high risk area. The high risk around changes in reserves has materialised which reflects this change.

Whilst these indicators are not highlighting anything that we are not already aware of, and they are not statements of fact – they are indicators that require continued and ongoing review.

It is also useful to note that the tool allows us to benchmark Woking against nearest neighbours and also upper tier councils.

CIPFA Financial Management Code

The Financial Management Code (FM Code) sets out the standards of financial management expected for local authorities. The Code builds on the CIPFA Prudential and Treasury Management Codes which require local authorities to demonstrate the long-term financial sustainability of their capital expenditure, associated borrowing and investments. The FM Code was launched in 2019 with the first full year of compliance from 2021/22.

Demonstrating this compliance with the FM Code is a collective responsibility of elected members, the Director of Finance and their professional colleagues in the leadership team. It is for all the Senior Management Team to work with elected members in ensuring compliance with the FM Code and so demonstrate the standard of financial management to be expected of a local authority.

The Council has not undertaken a review of its compliance with this CIPFA Financial Management Code as of the date of this report. The Council will need to programme in a review in 2023/24 as part of its delivery of the MTFS strategy.

The FM Code applies a principle-based approach. The principles are:

- Organisational leadership – demonstrating a clear strategic direction based on a vision in which financial management is embedded into organisational culture.
- Accountability – based on medium-term financial planning that drives the annual budget process supported by effective risk management, quality supporting data and whole life costs.
- Financial management is undertaken with transparency at its core using consistent, meaningful and understandable data, reported frequently with evidence of periodic officer action and elected member decision making.
 - Adherence to professional standards is promoted by the leadership team and is evidenced.
 - Sources of assurance are recognised as an effective tool mainstreamed into financial management, including political scrutiny and the results of external audit, internal audit and inspection.

Section Three of the code is particularly important as it covers the need for a long-term approach to the evaluation of financial sustainability, recognising that short-termism runs counter to both sound financial management and sound governance. The following paragraphs set out the Financial Management standards in this area.

Standard F - The authority has carried out a credible and transparent financial resilience assessment - The CIPFA Financial Resilience Index has been developed to enable organisations to identify pressure points.

The index is not intended to represent the entire story on the financial sustainability of a Local Authority but provides some indicators of potential risk. The Director of Finance has examined the major assumptions used within the budget calculations and associated as covered in this Section 25 report.

Standard G - The authority understands its prospects for financial sustainability in the longer term and has reported this clearly to members. - This report sets out the longer term financial strategy and how financial sustainability is being maintained. It is also demonstrated by the Section 25 statement within this report.

Standard H - The authority complies with the CIPFA Prudential Code for Capital Finance in Local Authorities. This includes information based on the proposed revenue and capital budgets, such as authorised and operational boundaries for debt and the maturity structure of the Council's borrowing.

Standard I - The authority has a rolling multi-year medium-term financial plan consistent with sustainable service plans. It is recommended best practice that Local Authorities have a longer-term strategy for financial resilience and a multi-year financial plan. Whilst the suite of budget reports are focussed on 2023/24 to align with the central government's Finance Settlement effective arrangements are in place to facilitate longer term financial planning including:

Five-year Capital Strategy (and financing arrangements) and asset management plans

- Three-year financial position and strategy for delivering a balanced budget set out in this report
- Financial and scenario planning over the next spending review period

Officers have tested that the new savings and mitigations identified for 2023/24 are deliverable with some risks. The Council's Risk Based Reserves Strategy provides for some slippage and under-delivery of savings plans. A detailed risk rated savings tracker is monitored and will be reported to the Corporate Leadership Team through the new performance monitoring arrangements that are being introduced in 2023/24 to replace the Green Book reporting.

Additionally, the governance process for investment and funding decisions for the Council's investment programme requires a clear and detailed business case for any proposed investment, which must explain the benefits of the project to the organisation, both financial and otherwise, alongside the funding requirement. This allows senior officers and members to make decisions on proposals based on value for money and other concerns, for example statutory requirements.

REPORT ENDS