Mayoral Combined Authority Board

21 March 2022

Annual Budget and Treasury Management Strategy 2022/23

Is the paper exempt from the press and public?	No
Reason why exempt:	Not applicable
Purpose of this report:	Governance
Is this a Key Decision?	Yes
Has it been included on the Forward Plan?	Yes

Director Approving Submission of the Report:
Gareth Sutton, Chief Finance Officer/s73 Officer

Report Author(s):
Gareth Sutton
Gareth.sutton@southyorkshire-ca.gov.uk

Executive Summary
This report proposes a budget and accompanying financial strategies for financial year 2022/23. The proposed budget provides resource totalling c. £472m to enable the activity required to deliver upon the objectives set in the MCA's Corporate Plan.

What does this mean for businesses, people and places in South Yorkshire?
The budget reflects the region's financial plan, determining where, when, and to what value investment is made available to support the delivery of its aspirations.

Recommendations
1. Approve the adoption of the revenue and capital budget estimates for the year;
2. Approve the Reserve Strategy;
3. Approve the Treasury Management Strategy;
4. Approve the award of CRSTS Revenue Grant;
5. Approve the award of capital grant from the Mayor's Sustainable Transport Fund;
6. Delegate authority to the Section 73 Officer to accept a number of grant awards.

Consideration by any other Board, Committee, Assurance or Advisory Panel

Audit and Standards Committee	27 January 2022
Mayoral Combined Authority Board	24 January 2022
Mayoral Combined Authority Board	15 November 2021
Mayoral Combined Authority Board	20 September 2021

1. Background

1.1 In common with other public bodies and local partners, the MCA Group is required to set a balanced budget every financial year. This budget must be approved by Members ahead of the new year and be supported by a medium-term financial strategy that takes account of forecast future expenditure, funding flows, and the requirements for use of reserves.

1.2 In support of this, the MCA has undertaken a Group wide integrated business planning process. This process seeks to derive resource requirements to deliver upon the aspirations set by the Member priorities and foundational strategies such as the Strategic Economic Plan and the Renewal Action Plan. The business plan in turn drives the budget by ensuring that financial resource is directed to business priorities.

1.3 In undertaking this activity at the Group level the MCA is better able to begin coordinating and aligning its Group wide financial and human resource to Group wide priorities. This supports a degree of business integration ahead of the formal integration process.

1.4 The budget estimates provided in this report reflect the levy funded activity of SYPTE, and the broader activity of the MCA and LEP. Expenditure related to support functions is shown in aggregate where possible, supporting greater transparency on the costs of delivering activity and statutory obligations across the Group.

1.5 Financial activity is presented along Thematic Board reporting lines, enabling oversight of funding and activity at this level at both budget setting and throughout the year as financial monitoring reports are prepared.

1.6 The budget proposals presented in this report are notable for a number of issues:

1. At c. £472m, the level of resource available for the region will enable record in-year levels of investment;
2. The commercial sustainability of the public transport network remains of critical concern, and whilst there is now an expectation of further government support the quantum and longevity is unknown;
3. Global issues continue to impact locally, with inflationary pressures now expected to provide challenges to the delivery of existing and emerging investment plans;
4. The funding environment remains challenging with a lack of clarity on a number of grant streams presenting income risk, and a lack of funding for core business aspirations inhibiting Strategic Economic Plan aspirations;
5. This budget provides resource to continue the development of the investment strategy and resource for delivery ready investment priorities, with this funding complemented by the expected receipt of borrowing powers, legislation for which is currently progressing through Parliament; and,
6. The medium-term outlook for the MCA is characterised by the need to consider levy increases to support core funding of existing activity, whilst there is a growing risk around the MCA's expected exposure to the financial and operational performance of the tram network post-2024.

1.7 As in the previous financial year the key immediate planning concern is the commercial sustainability of the public transport network. With fare-paying patronage still well below sustainable levels and with committed government funding due to end in early April, the risk that services begin to be withdrawn is acute.

1.8 Whilst there is now an expectation that funding will continue beyond the current commitment there is no certainty on quantum or longevity. The lack of longer-term planning at the national level will continue to inhibit planning at the local level.

1.9 This report notes the financial strategy to support this risk – as agreed at the January Board - including the re-deployment of forecast concessionary fare savings to tendered services and the availability of reserves. Managing the transition to a sustainable service levels will remain a formidable challenge.

1.10 The report also notes the record level of resource available to the MCA in the new year at c. £472m. Whilst this level of resource provides significant opportunity and reflects the scale of investment into the region, the quantum also carries significant delivery risk.

1.11 That delivery risk is likely to be exacerbated by the challenges in the supply-chain and labour-markets, as global forces continue to drive inflationary increases across most expenditure lines. These matters are likely to affect both the pace and cost of delivery.

1.12 The report further notes the lack of clarity on funding streams as we approach the new financial year. This is particularly prominent on the major City Region Sustainable Transport settlement, the envelope for which was initially announced in October, and a number of core income streams. This lack of clarity inhibits planning, with uncertainty not just around the level of investment achievable but the mobilisation of teams and systems to deliver that investment.

1.13 Gainshare resource is provided through the budget for investment in capacity and the development of investment plans across all partners, with capital resource made available to support delivery ready schemes. An element of revenue is reserved to support borrowing should additional investment headroom be required.

1.14 Finally, the report notes the challenging medium-term environment. The current strategy of releasing the Levy Reduction Reserve to offset against a falling cost-base is likely to become unsustainable by 2025/26 as inflationary cost pressures offset the savings made from retiring legacy debt. Consideration will need to be given to levy increases in the next budget cycle to avoid a cliff-edge once the reserve is exhausted.

1.15 The challenge of sustaining the MCA’s core transport activity will likely become more acute as the realities of the end of the current tram concession in March 2024 become clear. New external forecasting suggests that left unmitigated the costs of sustaining the tram network will be materially in excess of previous forecasts.

1.16 Work is underway to shape an appropriate operating modelling for the tram operations that mitigates the operating and financial risk that the MCA will otherwise become exposed to. Consideration will also need to be given to options to both grow tram patronage and manage the cost-base.

1.17 To support the budget, the report requests delegated authority for the Section 73 Officer to accept a number of cyclical grants that are expected to be offered to the MCA before the next Board meeting. Approval to award grants to the local authority partners are also sought.

2. Key Issues

2.1 This section of the report includes summaries of:

1. The Group Business Planning process which formed the requirement for the budgeted resource;
2. Budget proposals, complemented with further detail contained in the appendices;
3. Medium-term financial estimates;
4. The Reserve Strategy, including proposals for release of reserves; and,
5. The Annual Treasury Management Strategy

2.2 The Section 25 statement is provided at the end of this report. Summaries presented in this report are accompanied by more detail in the appendices.

<u>Group Business Planning Process</u>

2.3 The Group wide budget proposals and medium-term financial forecasts presented in this report have their foundation in Business Plans prepared across the Group.

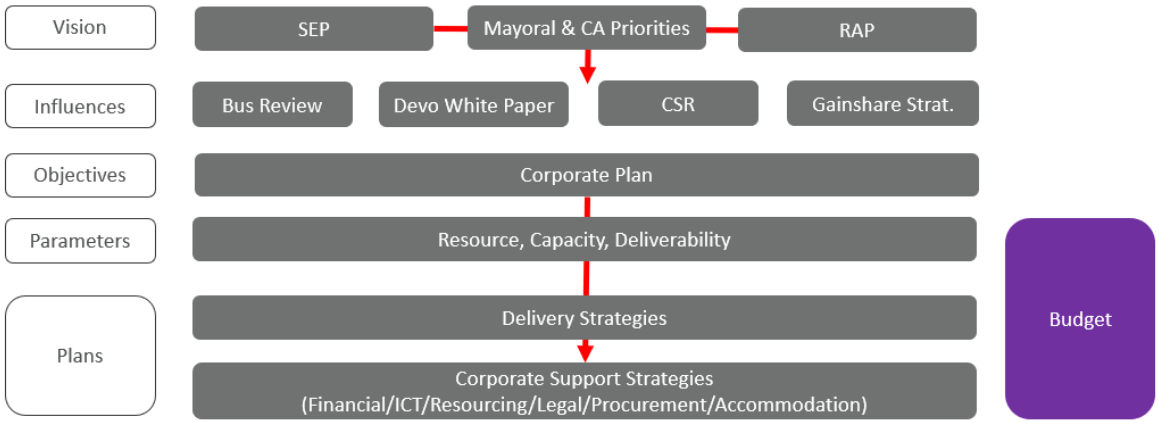
2.4 Recognising the MCA's commitment to implementing the Bus Review's recommendation to merge SYPTE into the MCA, an integrated Group wide business planning process was adopted for the first time ahead of this year's budget setting process.

2.5 This exercise has provided corporate focus on the objectives for the year, helped shape activity plans, and allowed for resource to be deployed to agreed priorities. The integrated approach across the Group has also supported better alignment in planning and use of shared resource.

2.6 The business planning process was fed from the MCA's anchor vision statements and influenced by a number of national policy issues such as the Spending Review, government's policy and fiscal response to the pandemic, and local policy issues such as the Bus Review and approaches to the deployment of devolution resource.

2.7 The Corporate Plan captured these issues and shaped agreed objectives for the coming year. Parameters for delivery plans were then set by the financial resource available and organisational capacity. These issues determine deliverability – what can be achieved.

2.8 The full process can be exemplified as follows:



2.9 A number of iterations of business plans were developed across the Group between October and February. At each stage the plans were adjusted to realign to the latest developments in our funding and operating environment.

2.10 Whilst much of the planning process involved the continuation of existing workstreams and programmes, the process also allowed focus to be placed on new and uncertain issues. This included:

- Consideration of the integration of SYPTE and the MCA, and the resource required to manage that change in an orderly and effective manner;
- Consideration of how the MCA will react to changes in the existing dynamic around emergency financial support to the public transport network;
- Consideration of how the MCA will react to potential changes in the regulatory environment that governs the relationship between bus operators and local public bodies;
- The emerging investment strategy and the resource required to support its planning and development;
- The adoption of new grant funding streams such as the City Region Sustainable Transport Settlement (CRSTS); and,
- Areas of emerging risk, particularly around the significant financial and operational risk that is likely to arise from the end of the current tram concession in 2024.

2.11 The planning process was set against continuing challenges around the MCA's core discretionary funding. At the time of writing there is still a lack of certainty on a number of core unrestricted funding streams, exacerbated by ongoing disruption to commercial revenues. This has impacted on the amount of resource that could be deployed in support of non-grant funded discretionary priorities such as policy development, marketing and communications, and the resourcing of certain thematic areas that don't attract discrete funding. Risk around the continuation of a number of critical grant streams – such as the LEP capacity grant – has been underwritten from reserves.

2.12 Using the Corporate Plan as an anchor, a rationing exercise was undertaken to align discretionary funding to key priorities. This has enabled the budget to be balanced, and for an appropriate use of reserves to be deployed, but it does mean that some aspirations have been deferred or displaced.

Budget Summary

Expenditure Plans

2.13 This report proposes a budget for the year of £472m, consisting of both revenue and capital expenditure. This expenditure will be resourced principally from discrete grants, with contributions, commercial income and the use of reserves supplementing:

Funding	£k	
Gross Expenditure	**£472,370**	
- Revenue	*£182,960*	39%
- Capital	*£289,411*	61%
Funded by:		
General Income	£4,774	1%
Release of Reserves and Provisions	£67,317	14%
Grants & Contributions	£400,279	85%
	£472,370	

2.14 This level of expenditure represents an increase of close to £103m (28%) on the prior year base budget:

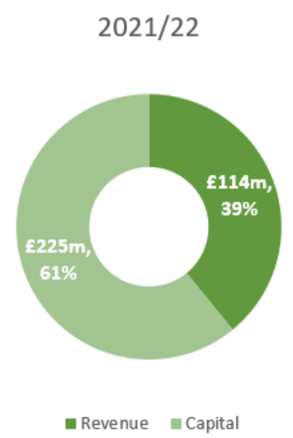
	2021/22 £k	2022/23 £k	Variance £k	Variance %
Revenue	£144,428	£182,960	£38,532	27%
Capital	£224,838	£289,411	£64,573	29%
	£369,266	**£472,370**	**£103,104**	**28%**

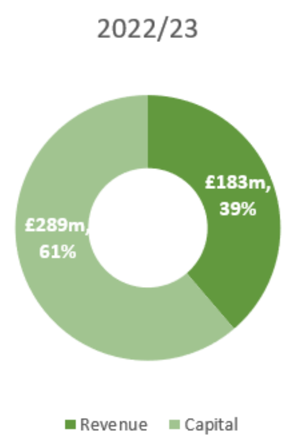
**restated*

2.15 The increase in resource largely reflects the coalescing of new grant streams with forecast slipped activity from 2021/22. The following table compares the proposed budget with the forecast outturn position, highlighting the significant increase in capital expenditure as previously planned activity now moves into the new financial year:

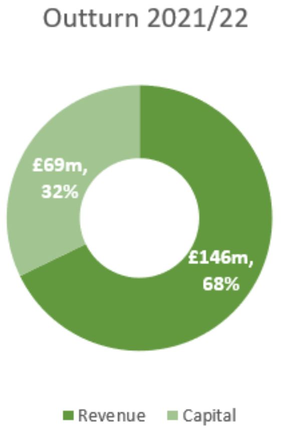
	2021/22 Outturn Forecast £k	2022/23 Budget £k	Variance £k	Variance %
Revenue	£145,545	£182,960	£37,415	26%
Capital	£69,024	£289,411	£220,387	319%
	£214,569	**£472,370**	**£257,801**	**120%**

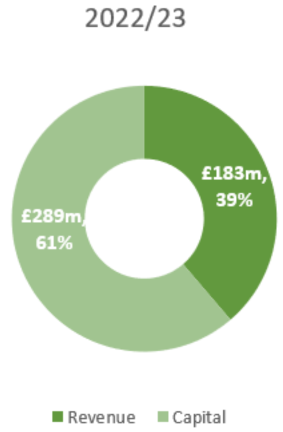
2.16 Whilst the adoption of new funding has increased the overall quantum of expenditure, the relative share of revenue and capital expenditure remains relatively unchanged between the 2021/22 base budget and the proposed 2022/23 budget:





2.17 However, when comparing against the forecast 2021/22 outturn position the impact of capital programme slippage becomes clearer:



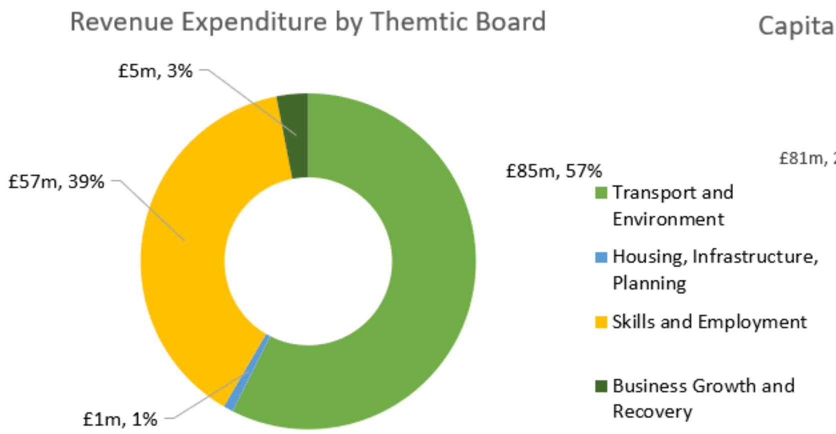


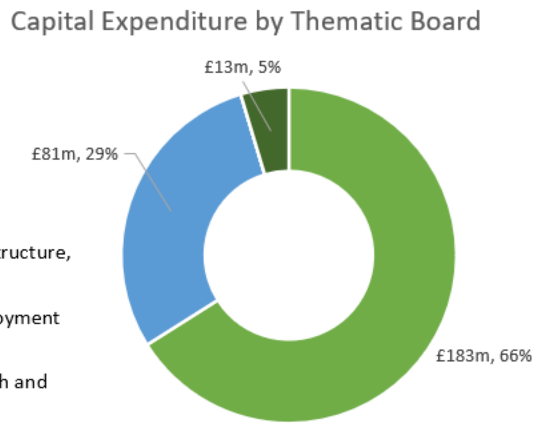
2.18 The movement of c. £140m of capital programme slippage from 2021/22 to the new financial year will present a significant delivery challenge for the MCA and partners.

2.19 The spread of expenditure across the Thematic Board areas largely reflects the ringfencing of grants to certain activity and the MCA Group's core competencies:

	Revenue £k	Capital £k	Total £k
Transport and Environment	£84,497	£182,605	£267,102
Housing, Infrastructure, Planning	£754	£81,012	£81,766
Skills and Employment	£56,664	£0	£56,664
Business Growth and Recovery	£4,485	£12,826	£17,311
	£146,400	£276,443	£422,843
MCA Executive	£32,421	£4,410	£36,831
Mayoral Office	£3,137	£0	£3,137
Uncommitted	£1,001	£8,558	£9,559
Total	**£182,959**	**£289,411**	**£472,370**

2.20 The differences in distribution between revenue and capital expenditure across the Thematic Board areas reflects the MCA's operational responsibilities for certain spheres of activity around transport, skills provision, and business support schemes:





2.21 The above graphic reflects that transport activity attracts significant amounts of revenue and capital resource, whereas skills and employment activity is exclusively revenue funded, and conversely housing and infrastructure is predominantly capital funded.

2.22 The graphic further exemplifies the relatively small amounts of funding for business growth activity relative to its importance to the Strategic Economic Plan and the region's aspirations. This is a significant issue for the region that shapes considerations around the deployment of unrestricted gainshare resource in particular.

2.23 The Transport and Environment portfolio includes the operational transport costs of SYPTE, largely funded by the levy and reserves. Whilst the cost of SYPTE activity is budgeted to remain relatively stable, this report does recognise the significant risks in this area, with resource held in reserves to help mitigate those risks. The financial strategy for the management of the commercial viability concerns for the transport network has previously been agreed and includes a freezing of the levy, redeployment of forecast concessionary savings to tendered service budget lines, and the ability to draw upon earmarked reserves. Additional also revenue resource is made available in this budget to support the costs of Bus Review activity and the expected costs of the Franchise Assessment. Capital expenditure in this portfolio reflects the transport maintenance grants and the significant investment via the Transforming Cities Fund that has now been rolled into the CRSTS programme. At this stage, the budget assumes that the MCA will receive the full allocation that was announced by the Chancellor in October, but at the time of writing this was still unconfirmed. Resource is also available via Active Travel grants complemented by gainshare contributions, whilst gainshare investment into bus infrastructure priorities and the final three months of the 18-21 travel concession is also included.

2.24 The Housing, Infrastructure, and Planning portfolio is a capital-intensive area. This principally reflects the inclusion in this portfolio of the Brownfield Housing and residual Getting Building grant funded activity along with the gainshare funding made available to local authority place investment into the region's towns and city. Revenue expenditure includes Net Zero activity, some non-capital Brownfield activity, and the costs of the development team. There will be significant focus in this area during the year on meeting deadlines set by Government for the utilisation of funding.

2.25 Conversely, the Skills and Employment portfolio is exclusively a revenue area. This reflects the adoption of the AEB activity, and the extension of the Working Win programme for a further year, along with MCA investment in apprenticeships and training programmes funded from devolved monies. In the prior year Getting Building Fund capital funding was used to support a number of the region's colleges, but this funding has now ended without a successor funding stream being announced.

2.26 A key area of concern for the region is the quantum of funding available to support business growth aspirations. In the new year, c. £17m of funding is expected to be applied, the majority of which relates to capital investment into businesses to support their growth. Following the end of the LGF programme and the delays to the launch of the Shared Prosperity Fund, there remains limited government funding in this area. The MCA has infilled around this deficit where possible with gainshare resource making up 61% of the funding available to the area in the new year.

2.27 Expenditure shown against the MCA Executive reflects the aggregate cost of the majority of the Group wide support functions. These functions are familiar to any public body and discharge the statutory responsibilities of the MCA, facilitate and manage the performance of the MCA's capital and revenue programmes, and provide the policy, assurance, communications, and strategic leadership for the Group. Much of these costs are recharged into programme funding to reflect their incremental nature. The ongoing uncertainty around the CRSTS allocation does mean that there is income risk around some of this activity.

2.28 Expenditure is inflated in the next financial year in this area by the forecast expenditure that will be necessarily incurred in preparation for the second Mayoral election in May 2022, and by a number of capital schemes seeking to improve and rationalise the MCA's estate. Over £12m of resource is also held in this area for the funding of the investment strategy proposals.

2.29 Expenditure incurred in the Mayoral Office reflects the staffing support provided to the Mayor, and Mayoral priority activity along with the Group's communications and external affairs teams. The direct costs of the Mayoral function are fully funded by the Mayoral Capacity Grant provided by Government. Communications and external affairs functions are funded from a variety of grants and other contributions, including the transport levy.

2.30 Reflecting the role of the MCA, the majority of the MCA's expenditure is incurred in direct investment into services via grant awards to partners for the delivery of programmes of activity, the payment of passenger and operator subsidies to public transport companies, and the delivery of projects. This is complemented by the cost of past financing decisions, people costs, the cost of premises including office accommodation and transport interchanges, and professional services:

	2021/22*		**2022/23**		**Variance**	
Expenditure Type	**£k**	**%**	**£k**	**%**	**£k**	**%**
Investment	£313,127	85%	£411,434	87%	-£98,307	-31%
Financing	£20,274	5%	£20,393	4%	-£119	-1%
People	£15,978	4%	£16,116	3%	-£138	-1%
Premises	£11,219	3%	£12,034	3%	-£815	-7%
Professional Services	£4,892	1%	£6,620	1%	-£1,728	-35%
Supplies & Services	£3,201	1%	£5,416	1%	-£2,215	-69%
Communications	£575	0%	£357	0%	£218	38%
	£369,266		**£472,370**		**-£103,104**	**-£1**

2.31 The spike seen in investment costs reflects the adoption of new grants coalescing with slipped activity, whilst the increase in professional services costs reflects the provisions made for the franchising assessment, bus review activity, and the project work around the end of the tram concession. Increases in the supplies and services largely reflects the cost of the Mayoral election, whilst the spike in premises related costs reflects in part the material inflation seen on utilities.

Funding

2.32 To fund the budget proposals, this report recommends the application of grants, and the deployment of general income and reserves.

2.33 Grants can be differentiated between those that are ringfenced, and those that are free from restrictions. Restrictions may arise from grant conditionality or from past MCA decisions to use grants (such as gainshare) for specific purposes.

2.34 This report proposes a funding package as follows:

Funding Sources	**£k**
Ringfenced/Committed Grants	
Revenue Grants	£146,149
Capital Grants	£254,130
	£400,279
Reserves & Provisions	
Capital Receipts	£35,280
Revenue Reserves	£32,037
Provisions	£0
	£67,317
General Income	
Retained Business Rates	£2,087
Local Authority Subscriptions	£1,184
Asset Management Trading Surplus	£459
Un-ringfenced Grants	£500
Income from Business Loans	£357
Investment Income	£188
	£4,774
Total Funding	**£472,370**

2.35 Whilst a large number, the release of revenue reserves and capital receipts largely reflects timing issues with grants received but not used flowing through to reserves and being drawn down in the following year.

2.36 Of most significance is the draw of £4.37m from the transport levy reduction reserve to support the freeze on the levy agreed at the MCA’s January Board. This freeze is in line with the current and proposed reserve strategy.

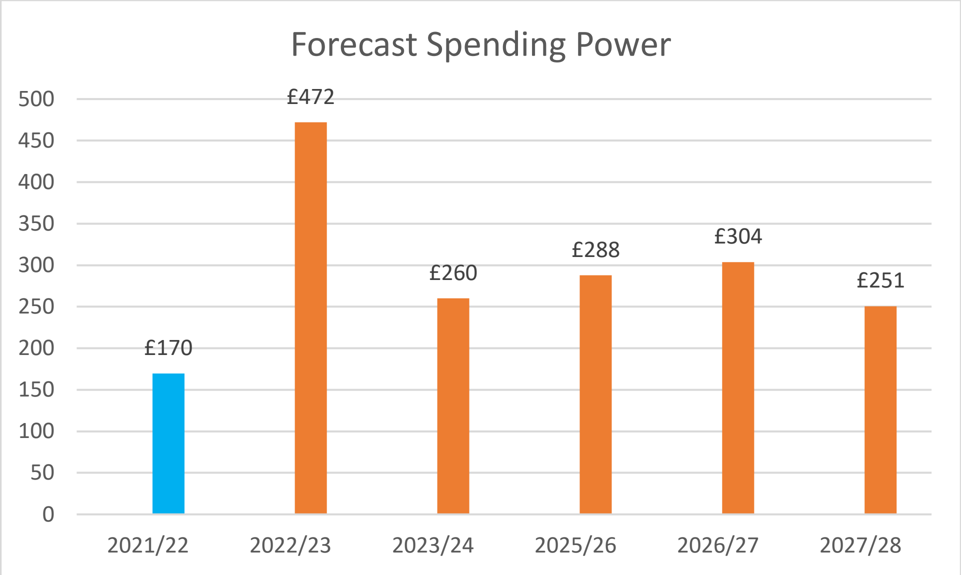
2.37 Freezing the levy and other local contributions results in calls upon the South Yorkshire local authorities as follows:

	Levy £k	**Subscriptions £k**	**Total £k**
BMBC	£9,530	£206	£9,736
DMBC	£12,017	£264	£12,281
RMBC	£10,180	£226	£10,406
SCC	£22,637	£488	£23,125
	£54,364	**£1,184**	**£55,548**

<u>Medium-Term Forecasts</u>

2.38 Forecasts of spending power in future years highlights that the resource available in 2022/23 will likely represent a peak. This peak reflects the new short-term funding made available in 2020/21 as part of the Government's fiscal response to the pandemic, but also the slippage of significant amounts of planned activity as restrictions, supply chain pressures and inflation all impacted upon delivery.

2.39 The following chart shows the forecast level of expenditure to 2026 based on known funding streams and known expenditure requirements:



2.40 The graphic above highlights a number of underlying movements.

2.41 Notably, expenditure in 2021/22 has, in part, been focussed on the delivery of pandemic related interventions funded by the government's fiscal response package. This includes Additional Restrictions Grant revenue used to support the South Yorkshire Business Support Scheme and the Getting Building Fund capital resource that has supported infrastructure development across the region. Grant conditions on the use of this funding require all resource to be expended by March 2022, encouraging delivery partners to focus on the immediacy of that target over other activity. This has led to significant amounts of slipped activity now moving into the new year.

2.42 Whilst ARG and Getting Building Fund monies will no longer be available in the new year, slippage will coalesce with new funding and other planned activity. Based on current profiling and the previously announced CRSTS funding envelope, up to £33m of CRSTS activity is budgeted for in the new year, which will complement existing TCF activity forecast at £138m alone.

2.43 Clearing the significant slippage in the new year should mean that the peak of expenditure falls significantly into 2023/24 before rising gradually as the CRSTS programme begins to pick up.

2.44 Profiling may also be affected by the emergence of new funding streams as the Government's levelling-up agenda begins to develop. No provision is made in these forecasts for potential distributions that may come to the region through the second round of the Levelling Up Fund nor the Shared Prosperity Fund.

2.45 The ability to shape the pace and timing of investment resourced from devolution monies will also be in the gift of the MCA once it is in receipt of borrowing powers. These powers are complementary to the long-term funding commitments and will allow the MCA to accelerate investment into the near-term, accruing the benefits of investment far sooner than if expenditure was matched to the 30-year profile of the devolution settlement.

2.46 At the time of writing the secondary legislation required to confer these powers upon the MCA was passing through Parliament. Provision is made within the 2022/23 budget to provide resource to support borrowing headroom of c. £40m.

2.47 As further detail becomes available on potential new funding streams and investment plans, the medium-term forecasts will be updated with budget revisions presented to Board on a quarterly basis.

Reserve Strategy

2.48 Regulation requires that the MCA adopts an annual reserve strategy. Reserves are held to mitigate risk, guard against financial shock, and provide available resource to meet opportunities.

2.49 The MCA holds reserves across the Group structure. These reserves are generally differentiated between capital and revenue amounts, and those that are earmarked to specific activity or otherwise.

2.50 Earmarked reserves are held to manage known issues, including the mitigation of identified risk or meeting the demands of forecast future resource requirements. Unearmarked reserves are held to provide the MCA with the ability to exploit opportunities that may arise, whilst also guarding against latent risk.

2.51 In 2021 the MCA undertook a significant reserve review across the financial Group. That review was prompted by both the integration of SYPTE and the MCA, and thus the requirement to better consolidate financial resource into a coherent strategy, and the need to consider how the Group’s financial resource could be brought to bear to support the mitigation of risk arising from the pandemic and in particular the viability concerns on the public transport network.

2.52 This review led to a major restructuring exercise, with reserves re-set to mitigate against known risks. New earmarked reserves were created to support the management of the Bus Review activity and the Tram Project, ensuring the Group properly prepares for the end of the current tram concession in 2024. A ‘Protection of Priority Services’ reserve was also created to ensure the MCA had available resource to support the transport network in the event of government subsidies being withdrawn before fare-paying patronage had returned to sustainable levels.

2.53 Income resilience reserves were also created across the Group to ensure that the MCA had a financial buffer against commercial revenue fluctuations, whilst resource was also earmarked for gainshare commitments.

2.54 This exercise complements the existing reserve strategy of releasing the transport ‘Levy Reduction Reserve’. This reserve was created from a financing restructure in 2015 and has been draw upon since 2015 to sustain reduction in the transport levy burden on local partners.

2.55 As part of the budget setting process for the new year the reserve strategy has again been reviewed. This review sought to achieve a number of key objectives:

1. An assessment of whether the quantum of reserves held was appropriate for the heightened risk in our operating environment;
2. An assessment of whether our reserves were mitigating the right risks; and,
3. An assessment of whether our reserve strategy appropriately supported our adapted financial strategy.

2.56 The exercise noted three prominent issues:

1. The carrying balance on the PFI reserve was now adjudged to be in excess of the risk it was mitigating;
2. The use of the Levy Reduction Reserve was now forecast to be unsustainable, as inflationary pressures began to outstrip savings generated from retiring expensive legacy debt; and,
3. Into the medium-term there would be a growing need to increase reserves to offset the potential for financial shock as the MCA becomes exposed to the financial performance of the tram network at the end of the current concession in March 2024.

2.57 The PFI reserve has been growing steadily over the last decade as credits received from government outstripped the cost of the unitary charge. This has largely arisen due to the benign inflationary environment that has prevailed since the 2008 recession, with the committed funding assuming a higher level of RPI.

2.58 Modelling undertaken shows that despite the recent spike in inflation, and even if inflation runs well over the Bank of England's target-rate, the balance of reserves will be in excess of need up to the end of PFI arrangement in 2042. Accordingly, there is a risk now that resource that could be used to good-effect is tied-up up unnecessarily.

2.59 This report proposes that the costs of the proposed Franchise Assessment be met from a one-off draw on this resource, with £3m un-earmarked from the reserve leaving a balance of c. £11.7m.

2.60 Throughout the year discussions with members and officers on transport levy strategy has focussed on the risk that the use of the Levy Reduction Reserve was becoming unsustainable. The core strategy around this reserve was based on requirements for the reserve falling over time as expensive legacy debt was retired. Whilst that debt is being repaid, the savings generated are – in part – being offset by inflationary pressures.

2.61 It is now forecast that the budget will continue to run with deficits when the reserve is exhausted around 2027. Discussions with members and officers have focussed on the need to consider gradual levy increases to avoid a cliff-edge. In the near-term this report proposes a £4.36m draw on the reserve to support the levy in 2022/23. This draw will take the reserve to £8.36m.

2.62 Work on how the tram will be operated and funded after the end of the current concession arrangements has also begun to build-up a picture of the potential financial consequences for the MCA.

2.63 Prior to the pandemic the tram had been running at losses of c. £1m p/a. These losses had been linked to the disruption of the re-railing works, and prior to that activity the operations had been run at a profit. However, the impact of the pandemic on patronage, and the likely disruption arising from the CRSTS funded renewals programme, means that it is likely that the tram will require ongoing financial subsidy for some time.

2.64 Prior financial planning had identified the need for up to £1.5m of financial support, but new modelling suggests that figure may be materially understated. Work undertaken by specialist consultants now suggests that without mitigation up to £4m p/a would be required on favourable assumptions, with up to £7m in adverse circumstances.

Work is underway to determine how these assumed deficits could be mitigated through priming patronage growth and/or reducing costs, whilst consideration is also being given to how different operating models could limit the MCA's overall exposure to the financial risk.

2.65 However, for financial planning purposes the scale of the challenge now needs to addressed through sustainable funding and through the management of reserves to mitigate the risk of adverse performance.

2.66 Supporting the future of the tram in the medium-term will need to be considered alongside near-term support to the bus and tram network in the event of government emergency funding ending in the new financial year.

2.67 In the immediate term the Protection of Priority Service reserve remains available for immediate deployment (£7m) whilst other reserves could be made available if the risks that those reserves mitigate is backed-off in other ways.

2.68 Reserve profiling for the new year continues to reflect timing differences between the receipt of grant and its deployment. In particular gainshare reserves have accumulated in the preceding two years but are now expected to be drawn upon in the new year as schemes come on-line and other funding is disbursed.

2.69 Release of revenue reserves will be complemented by the release of capital receipts to fund capital expenditure. This largely relates to the funding of the tail of the LGF over-programming position and is resourced from recycled LGF funding held as receipts.

Annual Treasury Management Strategy

2.70 Regulation and the MCA's Constitution require that the MCA approve the adoption of an Annual Treasury Management Strategy (TMS).

2.71 The TMS sets the parameters within which the MCA will deliver its cash and debt management activities. The proposed TMS is appended to this report and includes an Investment Strategy and Prudential Indicators. Progress against this proposed strategy will be reported to the MCA at the mid-year point, and again at outturn.

2.72 In common with most other public sector bodies, the MCA's approach to its Investment Strategy is governed by a hierarchy of considerations centred on protecting public funding. This hierarchy places a greater emphasis on the security and the liquidity of the MCA's investments than it does on the yield generated from them.

2.73 This relatively conservative approach limits the MCA's exposure to losses arising from counterparty default, but also limits the returns that can be generated from investing cash resource until it is required.

2.74 Noting the significant financial uncertainties prevailing in financial markets the TMS proposes to maintain the current stance, limiting investments to the safest of counterparties.

2.75 Whilst interest-rates remain historically low, it is now forecast that rates will begin to rise improving investment income returns. This factor, along with forecasts showing elevated cash balances, has meant that the MCA is now forecasting a marginal increase in the revenue it generates from investing cash held in advance of need.

2.76 The TMS also notes the intention to retire a further £8m of borrowing during the year, following the £61m repaid in the preceding two years. The repayment of this borrowing reduces the cost of debt by c. £0.39m.

2.77 The ongoing retirement of legacy debt will reduce the overall burden of financing costs on the revenue budget and the transport levy. This trend is matched to the release of reserves from the Levy Reduction Reserve, meaning that when that reserve is exhausted the cost of debt will have fallen so significantly that the reserve subsidy can be withdrawn on a sustainable basis.

2.78 Of note in the TMS is the proposed Minimum Revenue Provision (MRP) policy statement. The statement notes the MCA's proposed means of paying down any debt associated with gainshare funded investment. The MCA proposes that for gainshare investment the annual gainshare capital allocation be used to pay down the capital finance requirement, obviating the need for a charge to revenue (MRP).

2.79 The MCA contends that this approach is prudent, affordable, and sustainable, supporting the matching principle with capital resource paying down capital debt. The TMS notes that a government consultation on the capital framework may – inadvertently – prohibit the MCA from operating this approach, instead requiring that a revenue contribution be made to pay down capital debt. The MCA has engaged government officials on this matter and formally responded to the consultation. The MCA is hopeful that this engagement will support amendments to the proposals set out in the consultation.

2.80 Finally, the proposed TMS supports the potential for the MCA to take on gainshare funded debt in the new year. These budget proposals afford £1m p/a in revenue headroom to support financing costs should opportunities emerge that require the MCA to invest above the capital available to it.

Grant Acceptances

2.81 The MCA expects to be in receipt of a number of grant offers that will support these budget proposals. These grant offers are not the subject of bids, but cyclical awards.

2.82 This report requests delegated authority for the Section 73 Officer to accept the offers on behalf of the MCA, subject to the conditions being acceptable.

2.83 The following offers are expected:

- Adult Education Budget 2023/24
- Gainshare 2023/24
- LEP Capacity 2023/24
- Growth Hub 2023/24
- Mayoral Capacity Funding 2023/24

- Working Win 2023/24
- Brownfield Housing 2

2.84 The details of any acceptances will be reported through the delegated authority reporting and budget monitoring reports.

Grant Awards

2.85 Earlier in financial year 2021/22 the MCA received grant funding from the Department for Transport for the delivery of the CRSTS programme (£5.20m) and as settlement for changes to previous capital commitments made through the City Deal in 2014 (£12m). A further tranche of CRSTS revenue is expected in 2022/23 at around £5m, although at this stage this allocation has not been confirmed.

2.86 This report seeks approval to disburse these funds through the award of grants to the local authority partners. It is proposed that:

1. CRSTS Revenue received in 2021/22 (£5.20) and any funding received in 2022/23 is disbursed in accordance with the final capital settlement allocations across all five partners; and,
2. The Mayor's Sustainable Transport Fund be distributed to priorities agreed with each individual area.

2.87 Final allocations for the CRSTS programme are expected to be received before the end of the year. Distributing the revenue in line with capital allocations will support the delivery of the programme. Engagement with local authority partners has led to the proposal to distribute the Mayor's Sustainable Transport Fund in the following way:

Authority	Value £k	Scheme
BMBC	£2,000	Town Centre Sustainable/Active Travel Improvements
DMBC	£2,800	Mexborough Interchange
RMBC	£2,000	Eastgate/Parkgate Connectivity
SCC	£2,200	City Centre Accessibility Scheme
MCA	£2,000	Transport Futures Development Fund
Region Wide	£1,000	Active Travel Crossings
	£12,000	

Section 25 Statement

2.88 The Local Government Act 2003 requires that the statutory finance officer comments on the robustness of estimates used to determine the budget and the adequacy of reserves.

2.89 The Group Section 73 Officer (Group Finance Director) notes the significant work undertaken across the Group to develop the Corporate Plan and service level Business Plans. This work has been championed and led by senior officers across the Group. This has provided a strong, focussed approach to defining a body of activity that can deliver upon the MCA's priorities as defined by its elected leadership.

2.90 This Business Planning exercise has enabled the MCA to match its resource to priorities, drive efficiencies, and continue to ensure that Group wide reserves are focussed on key risks.

2.91 The Section 73 Officer notes the multi-disciplinary approach to forecasting activity, risk, demand for services, and financial profiling. This has led to informed budgeting and the proactive management of a number of emerging issues.

2.92 Reserves continue to be held at prudent levels for the management of current latent risk, whilst the reserve review undertaken as part of the budget setting process has allowed for a re-set of earmarked reserves.

2.93 Whilst the budget setting process and level of reserves allows for the MCA to approach the new financial year with a degree of confidence, a number of risks remain.

2.94 Principally, there are persistent concerns around the commercial sustainability of the South Yorkshire public transport network. The key variables in this equation – a return of fare-paying patronage and the longevity and level of Government funding – remain outside of the MCA’s direct control.

2.95 Whilst agreement has been reached to freeze the transport levy, and additional resource is provided within the revenue budget and within earmarked reserves, the scale of the potential challenge is likely to be beyond the MCA’s ability to manage without sustained Government support.

2.96 The MCA’s broader activity in the longer-term remains heavily reliant on Government funding cycles. Whilst long-term commitments to transport funding via the CRSTS package are welcome, the region does remain sensitive to Government policy decisions. The lack of funding for business activity is a key concern.

2.97 This report also notes that the budget proposed is set assuming a certain level of funding that has yet to be committed to. The lack of clarity from Government on a number of core funding streams is an impediment to good planning. For the purposes of this exercise the risk of funding not being forthcoming will be managed against General Fund reserves.

2.98 Work to design a new South Yorkshire investment strategy is essential to ensure the region is able to design and implement financial plans that will allow the MCA to bridge gaps in the Government’s investment cycles, avoiding exposure to boom-and-bust cycles that would impact on the organisation.

2.99 Looking ahead, in the medium-term the MCA will need to act on known sustainability issues associated with its local transport activity. The requirement to consider increases to the transport levy, or difficult policy choices, will be paramount in the new financial year to avoid a sustainability cliff-edge as the Levy Reduction Reserve nears exhaustion.

2.100 Finally, a financial and operational delivery plan will be required in the new financial year to address the implications of the end of the tram concession in 2024. The requirement to take direct responsibility for the operational and financial performance of the tram system in two years’ time could have profound implications for the MCA.

2.101 Identifying sustainable funding and an appropriate level of reserves will be critical to ensuring that the exposure to the risks of the system can be appropriately mitigated.

2.102 It is the opinion of the Section 73 Officer that these budget proposals are robust and provide a sound basis for the delivery of the MCA’s activity. The Section 73 Officer further believes that the current quantum of reserves held are appropriate and have been earmarked to mitigate key risks. The Section 73 Officer notes the significant challenges in the medium-term planning environment related to the operation and funding of tram operations from March 2024.

3. Options Considered and Recommended Proposal

3.1 **Option 1**
Accept the recommendations of this report

3.2 **Option 1 Risks and Mitigations**:
Acceptance of this report will support the delivery of the budget proposals.

3.3 **Option 2**
The recommendations in this report could be rejected.

3.4 **Option 2 Risks and Mitigations:**
It is a statutory requirement for the Board to adopt a balanced budget ahead of the new financial year.

A decision not to delegate authority to the Section 73 Officer for the award of grants could result in delays to the receipt of required funding.

3.5 **Recommended Option**
Option 1

4. Consultation on Proposal

4.1 The proposals in this report are the result of reports to the Board in September, November and January with one-to-one engagement with the Board members in November.

4.2 The Audit and Standards Committee were consulted on the Treasury Management Strategy in January.

5. Timetable and Accountability for Implementing this Decision

5.1 This budget will be live from April 2022.

6. Financial and Procurement Implications and Advice

6.1 This is a finance report the details of which are presented in the main body of the document.

7. Legal Implications and Advice

7.1 It is a legal requirement to set a balanced budget ahead of the new financial year.

8. Human Resources Implications and Advice

8.1 None.

9. Equality and Diversity Implications and Advice

9.1 None.

10. Climate Change Implications and Advice

10.1 None.

11. Information and Communication Technology Implications and Advice

11.1 None.

12. Communications and Marketing Implications and Advice

12.1 None.

List of Appendices Included:

A Budget Detail
B Treasury Management Strategy

Background Papers
None