Review of the Council's Arrangements for Securing Financial Resilience for Bath and North East Somerset Council

Year ended 31 March 2013

30 September 2013

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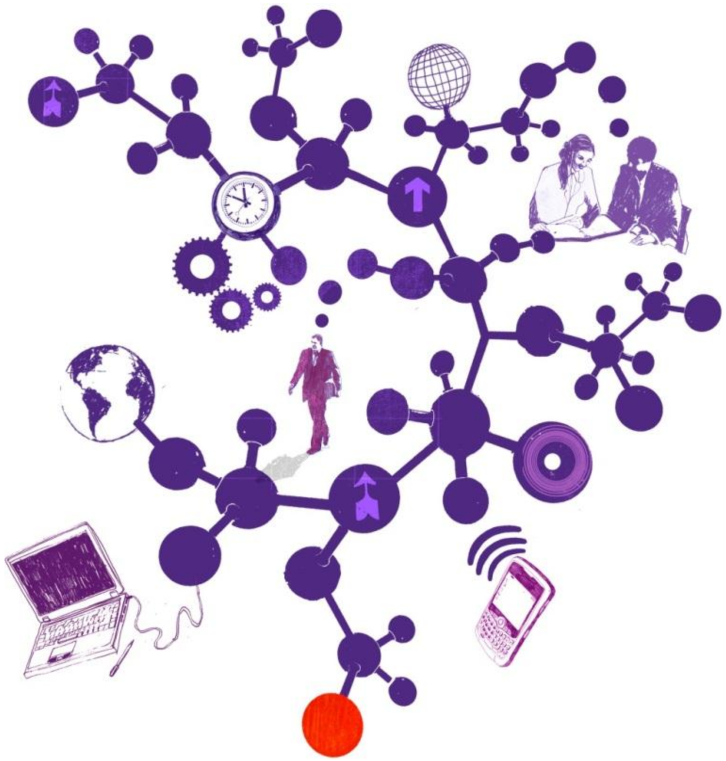

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Our approach

Value for Money Conclusion

Our work supporting our Value for Money (VfM) conclusion, as part of the statutory external audit, includes a review to determine if the Council has proper arrangements in place for securing financial resilience.

In so doing we have considered whether the Council has robust financial systems and processes in place to manage its financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future. We have carried out our work in discussion and agreement with officers and completed it in such a way as to minimise disruption to them.

The definition of foreseeable future for the purposes of this financial resilience review is 12 months from the date of this report.

We have reviewed the financial resilience of the Council by looking at:

- Key indicators of financial performance;
- Its approach to strategic financial planning;
- Its approach to financial governance; and
- Its approach to financial control.

Further detail on each of these areas is provided in the sections of the report that follow.

Our overall conclusion is that the Council has satisfactory arrangements in place to ensure financial resilience.

We have used a red/amber/green (RAG) rating with the following definitions.

Green	**Arrangements meet or exceed adequate standards**. Adequate arrangements identified and key characteristics of good practice appear to be in place.
Amber	**Potential risks and/or weaknesses**. Adequate arrangements and characteristics are in place in some respects, but not all. Evidence that the Council is taking forward areas where arrangements need to be strengthened.
Red	**High risk**: The Council's arrangements are generally inadequate or may have a high risk of not succeeding

Executive Summary

National and Local Context

National Context

The Chancellor of the Exchequer announced the initial Spending Review (SR10) to Parliament on 20 October 2010. SR10 represented the largest reductions in public spending since the 1920s. Revenue funding to local government was to reduce by 19% by 2014-15 (excluding schools, fire and police). After allowing for inflation, this equates to a 28% reduction in real terms with local government facing some of the largest cuts in the public sector. In addition, local government funding reductions were frontloaded, with 8% cash reductions in 2011-12. This followed a period of sustained growth in local government spending, which increased by 45% during the period 1997 to 2007.

The Chancellor of the Exchequer, in his Autumn Statement in November 2011, announced further public spending reductions of 0.9% in real terms in both 2015-16 and 2016-17. In his Autumn Statement on 5 December 2012, the Chancellor reinforced austerity measures announcing a further £6.6bn of savings during 2013-14 and 2014-15. Whilst health and schools will be continue to be protected in line with the Government's policy set out in SR10, local government will continue to face significant funding reductions. The Department for Communities and Local Government will contribute £470m of these additional savings, £445m of which will come from local authority funding during 2014-15, with local authorities being exempt from additional savings in 2013-14. In his March 2013 Budget the Chancellor announced further departmental 1% savings during each of 2013-14 and 2014-15. The NHS and schools remain protected, but police and local government will need to find an additional 0.5% over both years.

The next spending round period, 2015-16, was announced by the Chancellor on 26 June 2013. Local government will face a further 10% funding reduction for this period.

These funding reductions come at a time when demographic and recession based factors are increasing demand for some services, and there is a changing demand for some services, such as car parking, where customers pay a fee or charge.

Financial austerity is expected to continue until at least 2018.

Local Context

Bath and North East Somerset (B&NES) Council reported in February 2013 that during the period 2011 to 2015 central government grant funding will be cut by 40%. This assessment will be affected further by the Chancellor's announcement in June 2013 of further austerity measures.

The Council has a major savings programme and is adopting a more zero based approach to developing its budget. It's overall aim being to protect front line services, avoid increases in council tax and invest in homes and jobs for local people.

Executive Summary

Overview of Arrangements

Risk area	Summary observations	High level risk assessment
Key Indicators of Performance	The Council has a good track record of managing its budget and is maintaining prudent levels of reserves, although schools balances are at the lower end of the range compared to similar councils. The Council is maintaining a suitable level of liquidity, although collection rates for National Non-Domestic Rates were below the Council's target levels. Sickness levels increased in the final quarter of 2012/13, although there is no underlying trend	Green
Strategic Financial Planning	The Council has an embedded financial planning process which links to its corporate plans and ensures engagement by all stakeholders. Issues are discussed fully during the planning process and risks are identified and analysed. There remain inherent risks in the medium term, for example the generation of new homes bonus is dependent on the building of new properties.	Green
Financial Governance	The Council has a good track record with regard to addressing risks and ensuring Members and officers have a full understanding of the context within which the Council operates.	Green
Financial Control	Overall the Council maintains a sound control environment including adequate financial systems and has good processes for developing its annual governance statement. Good arrangements are in place for monitoring the achievement of savings, although the delivery of some of these savings remains challenging and targets are not always achieved. The asset register reporting modules require improvement to support the production of clearer reports. The Council is considering options for the future delivery of its internal audit service. Resources within the internal audit service dropped recently to 6.5 full time equivalents, against an establishment of 9.0 . Officers are looking recruit back up to establishment.	Green

Executive Summary

Next Steps

Area of review	Key points for consideration	Responsibility	Timescale	Management response
Key Indicators of Performance	• The Council should monitor its performance for the collection of National Non-Domestic Rates. • The Council should continue to monitor and address its levels of sickness. • The Council should continue to review the level of school balances and liaise with schools to ensure they remain adequate.			
Strategic Financial Planning	• The Council should continue to ensure its financial planning process is flexible and reactive to ensure the Council maintains a robust medium term financial plan.			
Financial Governance	None arising.			
Financial Control	• The Council should ensure arrangements for managing, monitoring and supervising the work of internal audit remain robust. • The Council needs to ensure sufficient officer resources are available to deliver agreed savings plans and ensure that risks are identified early and appropriate action taken to address them. • The Council should strengthen arrangements for obtaining reports from its fixed asset register to improve the financial reporting process.			

Key Indicators

Introduction

This section of the report includes analysis of key indicators of financial performance, benchmarked where this data is available. These indicators include:

- Working capital ratio
- Long term borrowing to tax revenue
- Long term borrowing to long term assets
- Sickness absence levels
- Out-turn against budget
- Useable Reserves: Gross Revenue Expenditure
- Schools Reserves - Balances to DSG allocations

We have used the Audit Commission's nearest neighbours benchmarking group comprising the following authorities:

Bedford Borough Council
Central Bedfordshire Council
Cheshire East Council
Cheshire West and Chester Council
North Somerset Council
Poole Borough Council
Trafford Metropolitan Borough Council
Shropshire Council
South Gloucestershire Council
Stockport Metropolitan Borough Council
Warrington Borough Council
Wiltshire Council
Isle of Wight Council
York City Council

Key Indicators

Overview of performance

We have assessed the Council across five areas. We have adopted a standard approach across all Councils to assist comparisons.

Area of focus	Summary observations	Assessment
Liquidity	Liquidity is the amount of cash or current assets the Council has to meet its short term commitments. Ensuring there is optimal liquidity enables the Council to operate efficiently. The Council's current assets exceed current liabilities in a ratio of 1.48 to 1. This is in line with the ratio maintained by other similar councils and indicates that B&NES is maintaining sufficient resources to meet short term liabilities reducing the risk of having to take on additional unexpected borrowing at short notice. The Council collected £145m in local taxes in 2012/13. Collection rates for council tax were in line with the Council's target of collecting 99% of the debit and above the national average of 97.4% as published by the Department for Communities and Local Government. Collection rates for National Non-Domestic Rates (NNDR) were 97.49% of the debit, below the Council's target of 97.8% and the average nationally of 97.7%. Had the Council met its target in NNDR collection in 2012/13 it would have recovered a further £192,000 on a debit of £62m.	Green
Borrowing	The Council's long term borrowing in relation to council tax and NNDR revenue is in the mid range compared to similar councils. Borrowing in relation to the asset base is slightly below average reflecting the Council's large asset base. The Council is meeting key targets. It's borrowing of £122m is below its capital financing requirement of £141.8m and the authorised borrowing limit set at £173m for 2012/13.	Green
Workforce	Sickness levels at the Council are below the national average (3.5days per year compared to 4.5).	Green

Key Indicators

Overview of performance continued

Area of focus	Summary observations	Assessment
Performance Against Budgets: revenue & capital	The Council has managed its spend within 2% of its original budget in each of the last 3 years which is a good performance. Actual spend in 2012/13 was £0.168m less the the revised budget of £122.9m. In 2012/13 there was slippage of £13m against the capital budget of £57m. This mainly related to re-phasing of schemes with few adjustments to the budgeted costs of individual schemes.	Green
Reserve Balances	The Council has a prudent level of reserves compared to similar councils. Earmarked reserves have increased over the last three years and the Council has plans to utilise some £16.4m of earmarked reserves over the next three years to support the costs of restructuring and affordable housing initiatives.	Green
Schools Balances	Schools balances are 4% of direct schools grant which is at the lower end of the range compared to similar councils.	Green

Strategic Financial Planning

Key characteristics of good strategic financial planning

In conducting our review of strategic financial planning we have assessed the Council's performance against the following indicators:

- Focus on achievement of corporate priorities is evident through the financial planning process. The MTFP focuses resources on priorities.
- The MTFP includes outcome measures, scenario planning, benchmarking, resource planning and details on partnership working. Targets have been set for future periods in respect of reserve balances, prudential indicators etc.
- Annual financial plans follow the longer term financial strategy.
- There is regular review of the MTFP and the assumptions made within it. The Council responds to changing circumstances and manages its financial risks.
- The Council has performed stress testing on its model using a range of economic assumptions including CSR.
- The MTFP is linked to and is consistent with other key strategies, including workforce.
- KPIs can be derived for future periods from the information included within the MTFP.

Strategic Financial Planning

Medium Term Financial Strategy (MTFS)

Area of focus	Summary observations	Assessment
Focus of the MTFS	The key Council objectives of protecting front line services and investing in homes and jobs are the main focus in the MTFS. Key aims and ambitions of the 3 year MTFS period such as supporting vulnerable people are set out, as are corporate assumptions such as ensuring balanced budgets with no on-going funding pressures and the adequacy of reserves. Equalities issues are considered.	Green
Adequacy of planning assumptions	Key planning assumptions are included in the medium term service resource plans developed each year in the autumn and in the overall summary budget report taken to Council each February. These include pay and contract inflation; unavoidable pressures such as IT costs and statutory changes such as to housing benefits administration grant. There are inherent risks in making assumptions but consideration is given also to possible changes in funding, changes in pension costs, changes in fees and charges and schools funding.	Green
Scope of the MTFS and links to annual planning	The annual budget report links to the MTFS and to the 'Change Programme'. The 'Change Programme' includes a range of initiatives reshaping services, working with partners and making better use of assets. The annual budget and MTFS incorporates the capital programme with links to the Treasury Management Strategy and other relevant plans such as the ICT strategy. The medium term service resource plans which support the MTFS further link to actions and strategies such as the workforce strategy.	Green
Review processes	The MTFS is reviewed each year as part of the Council's annual budget setting process. It takes account of policy developments locally and nationally, progress with the change programme and internal and external consultation.	Green
Responsiveness of the Plan	The MTFS includes a range of savings proposals developed by each service which were analysed and appraised before the Plan is finalised. The Council's Change Programme incorporates a range of actions to improve community engagement, reshaping services and improving the use of assets.	Green

Financial Governance

Key characteristics of effective financial governance

In conducting our review of financial governance we have assessed the Council's performance against the following indicators:

Understanding

- There is a clear understanding of the financial environment the Council is operating within:
  - Regular reporting to Members. Reports include detail of action planning and variance analysis etc.
  - Actions have been taken to address key risk areas.
  - Officers and managers understand the financial implications of current and alternative policies, programmes and activities.

Engagement

- There is engagement with stakeholders including budget consultations.

Monitoring and review

- There are comprehensive policies and procedures in place for Members, Officers and budget holders which clearly outline responsibilities.
- Number of internal and external recommendations overdue for implementation.
- Committees and Cabinet regularly review performance and it is subject to appropriate levels of scrutiny.
- There are effective recovery plans in place (if required).

Financial Governance

Understanding and engagement

Area of focus	Summary observations	Assessment
Understanding the Financial Environment	The annual budget pack taken to Cabinet and Full Council in February each year to support the budget and council tax setting decisions provides a detailed commentary on the financial environment and the challenges and risks faced by the Council. The budget process starts in early autumn with the development of medium term service resource plans which are reviewed by Policy Development and Scrutiny Panels, this also involves an overview of the financial environment. Seminars are held for Cabinet in January to explain key issues in advance of the formal meeting. 'Budget fairs' are held with stakeholders to discuss key issues as part of the financial planning process.	Green
Executive and Member Engagement	Directors and Cabinet receive a monthly briefing on finance matters. The Director of Finance attends senior management team and Cabinet. Reports cover progress with budgets and key issues arising, for example progress with the 'City Deal'. Reports include progress with the savings plan.	Green
Overview for controls over key cost categories	Financial responsibilities are set out in the Council's constitution. Progress with the budget is monitored in Cabinet reports analysed by Portfolio and for the capital programme analysed by scheme. Monthly dashboards to Cabinet include budget monitoring information by directorate. The reports are high level but provide explanations of the key issues and actions.	Green
Budget reporting: revenue and capital	Budget reports include forecast outturn and a summary of key issues including spending pressures and progress with income targets. Dashboards includes graphs and tables to focus on key risks.	Green
Adequacy of other Committee/ Cabinet Reporting	The Corporate Audit Committee receive regular annual reports on treasury management. Treasury management is an important area for the Council given is medium term plans to increase borrowing and achieve savings from improvements in use of funds. Treasury management reports include detailed background information such as information on risks, borrowing limits, prospects for interest rates (informed by the Council's advisors) and an economic commentary. Corporate Finance maintain a detailed record of progress with savings plans. Progress with key savings plans is included in budget reports to Cabinet. Reports include details of carry forword requests. The financial information is incorporated in an overall pack of information covering performance and finance.	Green

Financial Control

Key characteristics of effective financial control

In conducting our review of financial control we have assessed the Council's performance against the following indicators:

Budget setting and budget monitoring

- Budgets are robust and prepared in a timely fashion.
- Budgets are monitored at an officer, member and Cabinet level and officers are held accountable for budgetary performance.
- Financial forecasting is well-developed and forecasts are subject to regular review.

Savings Plans

- Processes for identifying, delivering and monitoring savings plan schemes are robust, well thought through and effective.

Financial Systems

- Key financial systems have received satisfactory reports from internal and external audit.
- Financial systems are adequate for future needs.

Finance Department

- The capacity and capability of the Finance Department is fit for purpose.

Internal Control

- There is an effective internal audit which has the proper profile within the organisation. Agreed Internal Audit recommendations are routinely implemented in a timely manner.
- There is a an assurance framework in place which is used effectively by the Council and business risks are managed and controlled.

Financial Control

Internal arrangements

Area of focus	Summary observations	Assessment
Budget setting and monitoring - revenue and capital	The budget is built up from detailed plans and has moved away from targets and top slicing to incorporate a greater focus on resourcing priority services and adopting a zero based approach. The approach challenges the allocation of resources. The budget setting process incorporates consideration of minimum reserves and the robustness of the budget taking account of the views of Directors and the section 151 officer. The Council's monitoring officer provides a report clarifying the process for approving the budget. Progress with the budget is reported monthly to senior management and Cabinet enabling actions to be taken quickly in relation to developing spending pressures.	Green
Performance against Savings Plans	In 2012/13 the Council planned for savings of £12m achieving £11.3. Mitigating actions totalling £0.25m were identified, leaving a net deficit of £0.5m. The budget includes detailed savings plans for the current year and following two years. The current year's budget 2013/14 includes savings of £11.63m. Actions to achieve savings are allocated to responsible officers who have to identify mitigating actions in the event of savings not being achieved. This may include bringing forward savings identified for future years, or alternative actions. Progress is monitored and managed at a corporate level. The Council has a good record of controlling costs and managing its overall budget. However, achieving the planned savings of £30m between 2013/14 and 2015/16 will be an on-going challenge.	Green
Key Financial Accounting Systems	Our review of key financial systems which included the documentation and walkthrough of key controls indicated the Council has generally adequate financial systems. Internal Audit reported in May 2013 that the Council's Internal Control framework and systems to manage risk are satisfactory. Internal Audit rate systems on a scale of one to five, with five being excellent. Only one of Internal Audit's systems reviews led to a rating of one, (poor) in respect of systems administration focussing on user access rights which is a key area of control. Actions have been agreed to strengthen the control environment and Internal Audit are following up their review in the current year.	Green

Financial Control

Internal and external assurances

Area of focus	Summary observations	Assessment
Finance Department Resourcing	The Council maintains a corporate finance team to support the Director of Finance covering the production of the annual accounts, budgets and medium term financial plans, VAT and technical and control functions. The Council has sought to build resilience in to its arrangements by ensuring knowledge and skill is spread across different members of staff. Additional finance officers are based in service departments who liaise with the Director of Finance in developing and monitoring budgets.	Green
Internal audit arrangements	Internal audit is staffed with experienced qualified personnel who follow a risk assessed plan. During 2012/13 80% of their planned programme was completed. Follow up reviews completed during the year indicated that 89% of recommendations had been implemented. Resources within internal audit have dropped recently due to staff turnover. During 2012/13 there were nine members of staff, this has reduced recently in July 2013 to 6.5 full time equivalents. Officers are planning to increase resources back up to the establishment of nine. The Council is considering options for the future provision of internal audit services and needs to ensure it continues to have a robust and resilient internal audit service.	Amber
External audit arrangements	Last year the Audit Commission's Audit Practice reported the Council had a satisfactory control environment and arrangements for preparing the accounts. External audit reported the need to continue to review accounting policies and consider setting a de-minimis level for treating items as capital expenditure. Officers have not felt it necessary to introduce a de-minimis level for capital but have continued to keep accounting policies under review. The need to improve the Council's asset register was also reported also, particularly the reporting modules on the system. Since last year officers have met the software supplier and reviewed overall arrangements for administering the fixed asset register including ensuring it is consistent with records held in Property Services. However , there remains scope to strengthen the reporting modules ensuring data can be downloaded to excel.	Amber
Assurance framework/risk management	The Council has a developed process for producing its annual governance statement which links to its risk management process, performance management systems and includes service assurance statements from Directors. The Annual governance statement is reviewed by the Corporate Audit Committee who also monitor progress with actions in respect of significant issues. The risk management process is embedded, with up-dates to the corporate risk register produced quarterly showing changes in RAG ratings and actions. The risk management strategy is reviewed by the Corporate Audit Committee. Risks are reported monthly to senior management and Cabinet focussing on key issues. Departments monitor their individual risk registers liaising with the Council's risk manager.	Green

Key Indicators of Financial Performance

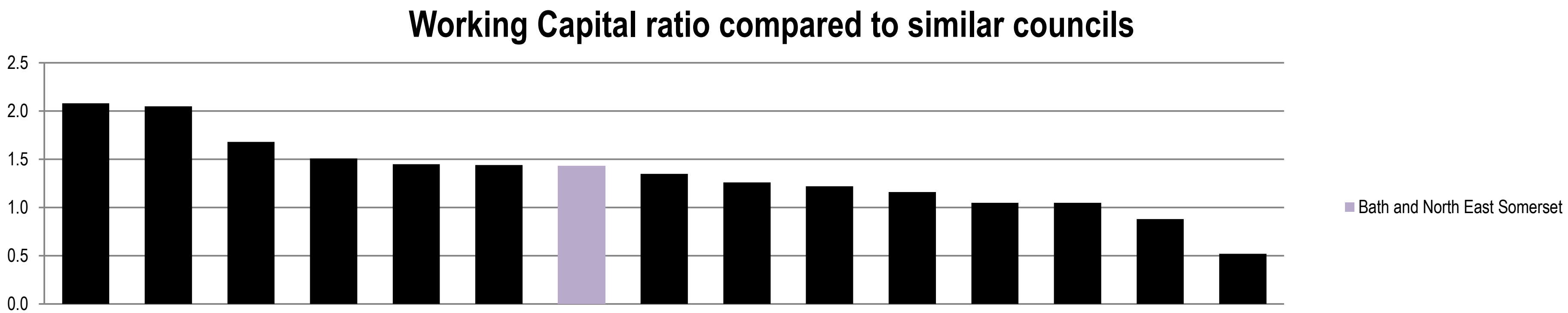
Working Capital - Benchmarked

Definition

The working capital ratio indicates if an authority has enough current assets, or resources, to cover its immediate liabilities - i.e. those liabilities to be met over the next twelve month period. A ratio of assets to liabilities of 2:1 is usually considered to be acceptable , whilst a ratio of less than one - i.e. current liabilities exceed current assets - indicates potential liquidity problems. It should be noted that a high working capital ratio isn't always a good thing; it could indicate that an authority is not effectively investing its excess cash.

Findings

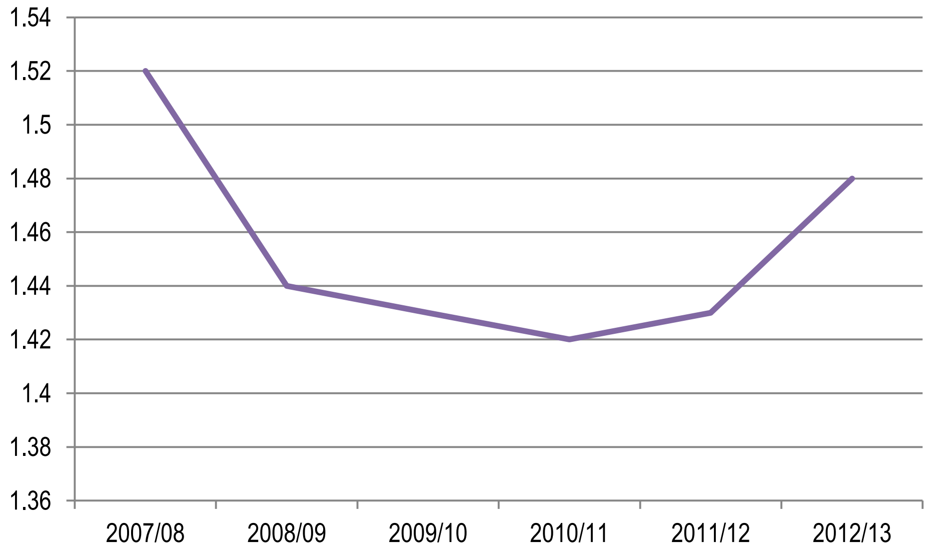
B&NES's working capital ratio has been relatively stable in recent years and stood at 1.48 to 1 at 31 March 2013 (1.43 to 1 at 31 March 2012). The following graph shows working capital in comparison to similar authorities using the audit Commission near neighbour group. (The comparative figures are for 2012). Working capital will come under increasing pressure during SR10 and will need to continue to be carefully monitored.



Source: Grant Thornton data base

Key Indicators of Financial Performance

Working Capital – Trend B&NES Council



Source: Grant Thornton data base

Over a 5 year period B&NES working capital ratio has remained relatively stable.

Key Indicators of Financial Performance

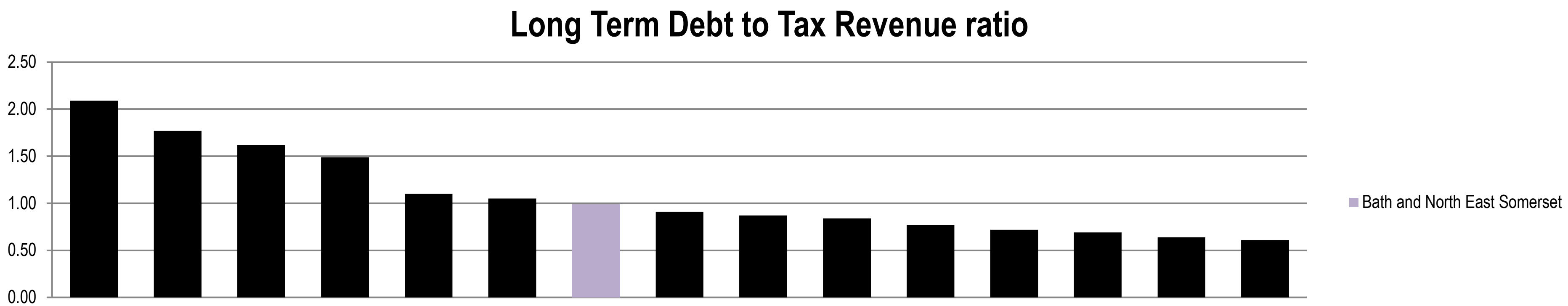
Long Term Borrowing to Tax Revenue - Benchmarked

Definition

Shows long tem borrowing as a share of tax revenue. A ratio of more than one means that long term borrowing exceeds council tax revenue.

Findings

B&NES long term borrowing is £122m, its income from council tax and redistributed national non-domestic rates in 2012/13 was £120.7m giving a ratio of approximately 1. The Council has no short term loans. This is in the mid range compared to similar authorities.



Source: Audit Commission's Technical Directory

Key Indicators of Financial Performance

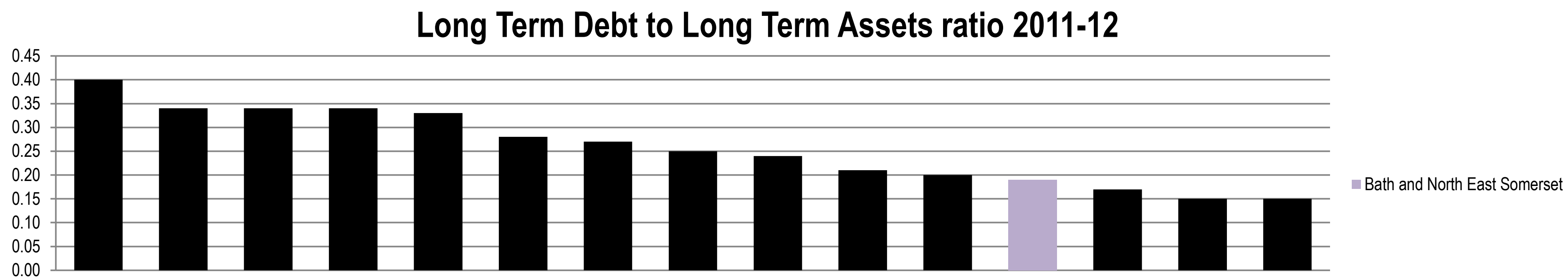
Long-term borrowing to Long-term assets - Benchmarked

Definition

This ratio shows long tem borrowing as a share of long term assets. A ratio of more than one means that long term borrowing exceeds the value of long term assets.

Findings

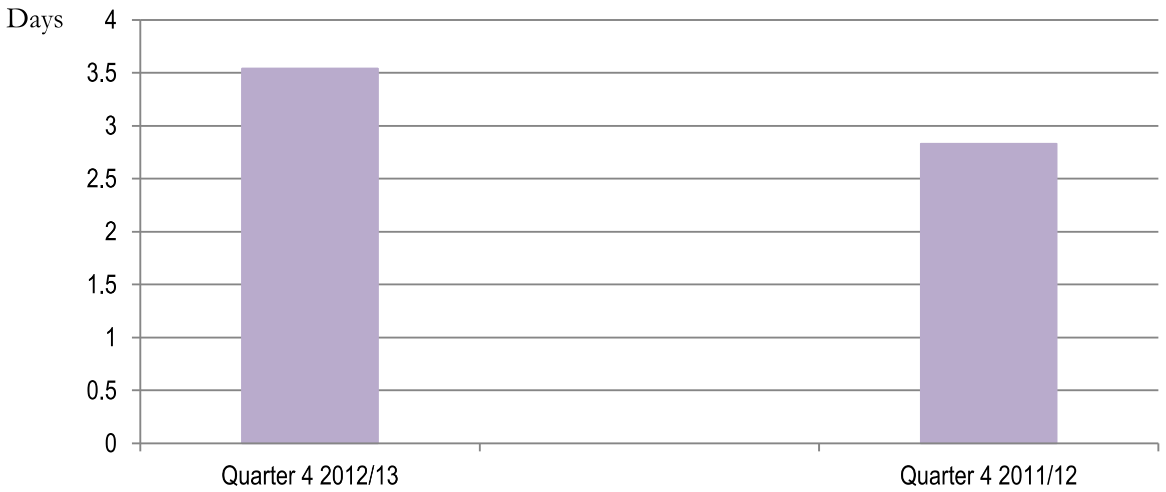
B&NES ratio at 31 March 2013 was 0.2, this is consistent with 2012 when it stood at 0.19. In relation to B&NES asset base the current level of borrowing is less than similar authorities. The 2013/14 capital budget envisages additional borrowing of up to £44.9m which would impact this ratio. This potentially would take borrowing from £120m to £165m. The value of the long term assets would be expected to increase but borrowing of £165m on existing long term assets of £587m would represent 0.28, the Council would still be in the mid range.



Source: Grant Thornton database.

Key Indicators of Financial Performance

Sickness Absence Levels



Source: B&NES performance report

The graph shows days lost per full time equivalent employee at B&NES Council.

The Office for National Statistic reported that the average number of days lost per worker across the economy in 2011, was 4.5. This is more than the days lost at B&NES which stood at 3.54 at the end of 2012/13.

Key Indicators of Financial Performance

Spend on non salaried staff and consultants (includes all spend in schools and interims)

Area of focus	2012/13 £'m	2011/12 £'m
Non Salaried agency staff	5.56	5.20
Overall payroll establishment	128.54	147.66
Spend on consultants	3.03	3.56

Source: B&NES accounts

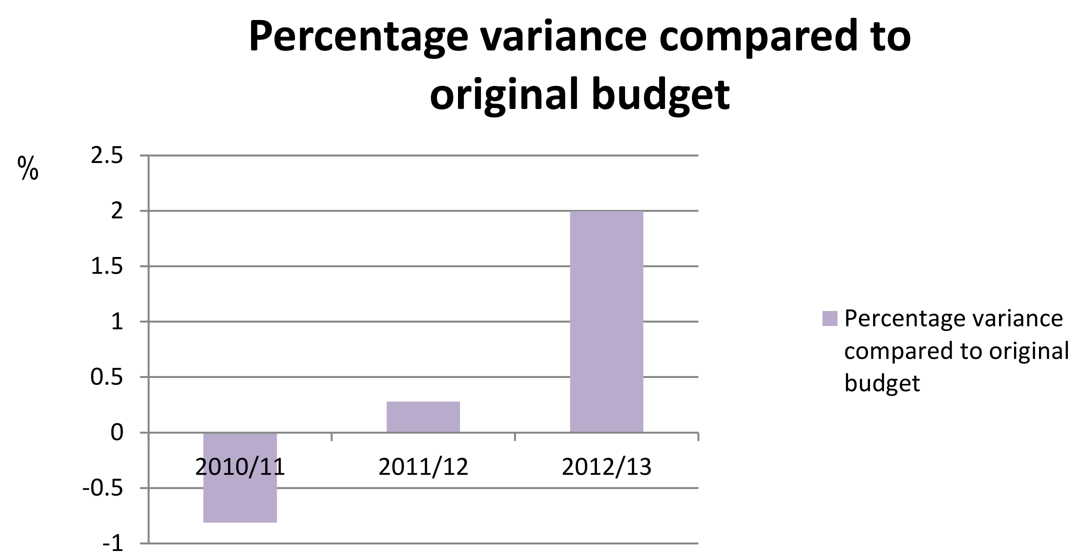
Payments to non salaried agency staff have remained relatively stable in the last two years despite the overall reductions in staff costs. These payments comprise a large number of relatively small amounts covering areas such as IT and staff seconded from the LGA.

Spend on consultants is across Council activities, the largest areas of spend included:

- Planning services £0.662m
- Customer Services £0.386m; and
- Health Commission and planning £0.269m.

Key Indicators of Financial Performance

B&NES performance against revenue budget



Source: B&NES accounts

B&NES has managed its spend to within 2% or less of its original budget over the last three years.

Within this there has been considerable pressure on income particularly from car parking causing overspends in net spend particularly with regard to the 'Place' Directorate.   In total there were net overspends of £1.7m on service budgets in 2012/13.

This has been offset in 2012/13 by underspends on corporate and agency budgets of £2m, the biggest element being an underspend of £1m on debt financing costs due to slippage in the capital programme. Similar underspends on debt financing have occurred in previous years. Overall the Council has maintained strong budgetary discipline.

Key Indicators of Financial Performance

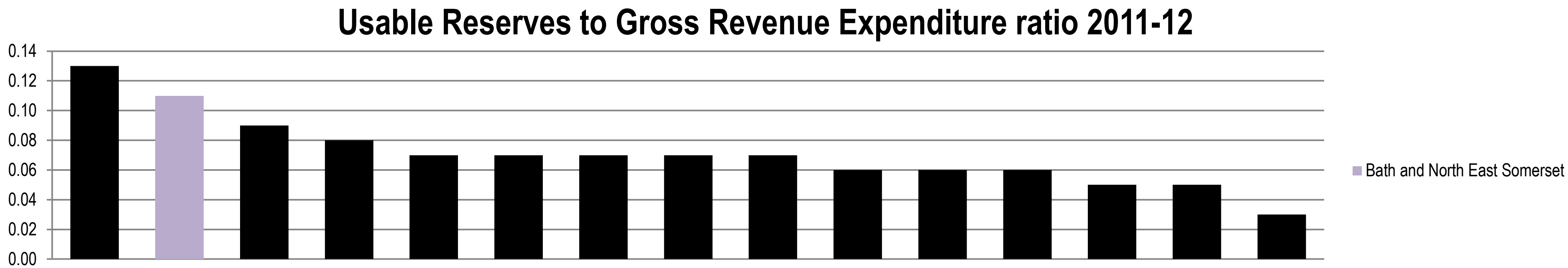
Useable Reserves - Benchmarked

Definition

This shows useable capital and revenue reserves as a share of expenditure. A ratio of one means the total reserves matches the level of expenditure.

Findings

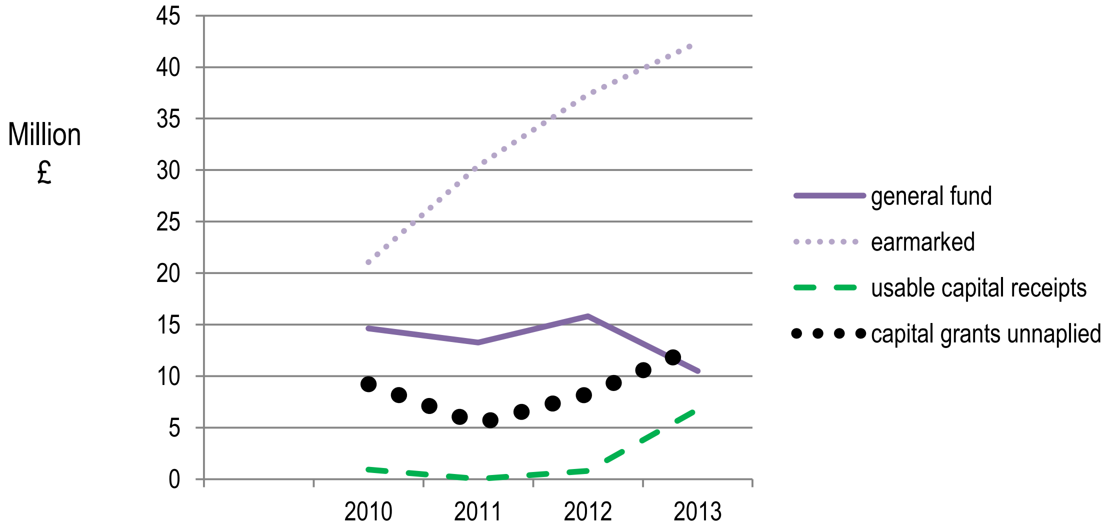
B&NES are maintaining a prudent level of reserves, higher compared to other similar authorities. The comparison below is to similar councils for 2011/12 being the most recent data available. The ratio of reserves to gross expenditure at B&NES has increased further in 2012/13 to 0.16, reflecting an increase in reserves of £10m to £72m and a reduction in gross expenditure to £449.6m. This needs to be set against the context of planned savings between 2013/14 and 2015/16 of £30m agreed by the Council and the subsequent Government announcement of further austerity measures announced by the Chancellor in June.



Source: Audit Commission's Technical Directory

Key Indicators of Financial Performance

Useable Reserves - Trend by Type



Source: B&NES accounts

Earmarked reserves include school balances, which at 31st March 2013 stood at £3.3m.

The Council has plans to utilise certain reserves. Within the MTFS there are plans to spend some £16.4m of earmarked reserves between 2013/14 and 2015/16. The MTFS also envisages general fund balances reducing by £1m over the same period.

Key Indicators of Financial Performance

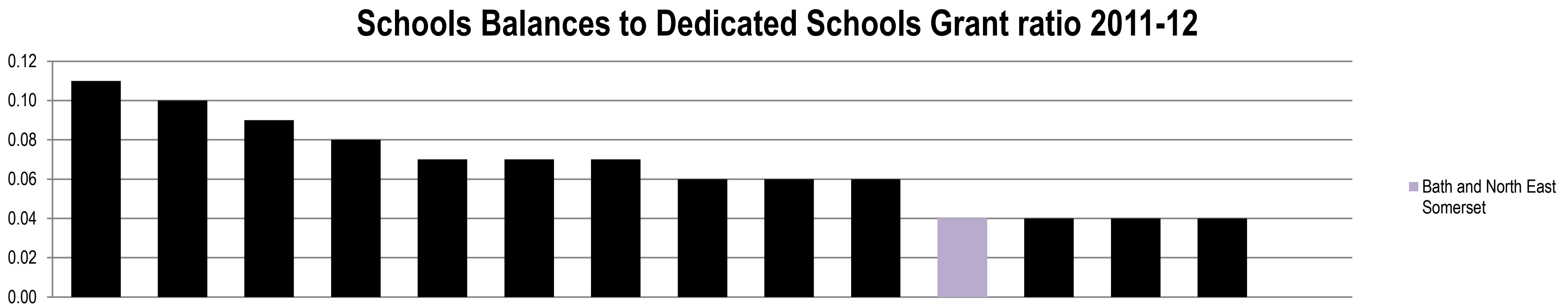
Schools balances to DSG allocation - Benchmarked

Definition

This shows the share of schools balances in relation to the total DSG allocation received for the year. For example a ratio of 0.02 means that 2 per cent of the total DSG allocation remained unspent at the end of the year.

Findings

B&NES ratio for 2012/13 and 2011/12 remained at 4%. This is at the lower end of the range compared to similar authorities.



Source: Grant Thornton data base

Grant Thornton

grant-thornton.co.uk