Local Government Act 2003: Section 25 Report by the Director of Finance

Introduction

1.1. The Local Government Act 2003 (Section 25) requires that when a local authority is agreeing its annual budget and precept, the Director of Finance (Sheila Little) must report to it on the following matters:

- the robustness of the estimates made for the purposes of the calculations; and
- the adequacy of the proposed financial reserves.

1.2. The Council must have due regard to the report when making decisions on the budget and precept.

1.3. In expressing her opinion, the Director of Finance has considered the financial management arrangements that are in place, the level of reserves, the budget assumptions, the overall financial and economic environment, the financial risks facing the County Council and its overall financial standing.

1.4. Strategically the financial and economic context facing the Council remains similar to recent years: according to the Office of Budget Responsibility (OBR) more of the funding cuts remain to be delivered than have already been introduced (60% still to come). Austerity is now clearly forecast to last for a decade up to 2020. The strategic messages and many of the risks, set out in this report, are therefore similar to last year. However, two particular features this year are:

- delivery is likely to be increasingly challenging in view of the continuing year on year growth in demand on services as a result of demographic demand pressures and reduction in funding; and
- the absence of a Comprehensive Spending Review beyond 2015/16. This makes medium term financial planning less certain. In response, a key difference for this MTFP (2015-20), is the plan to review the budget in the summer 2015 and report back to Cabinet.

1.5. Preserving the Council's financial resilience remains the key long-term driver in the council's financial strategy as the Council moves forward to the next 5 year MTFP (2015-20).

1.6. The Council has successfully delivered significant efficiency savings & service reductions in each of the last four financial years (2010/11 £68m, 2011/12 £61m, 2012/13 £66m, 2013/14 £62m), and is forecast to deliver further savings for 2014/15 of £69m. Adding this to the additional funding and savings included in the budget assumptions for the next MTFP (2015-20) makes a total of £588m over the decade. Throughout this period the Council has continued to drive for increased improvement, added value and reduced unit costs (and the latest unit cost booklet is attached in Appendix 1).

1.7. As indicated previously, the level of savings delivered continues to retain a balance of approximately an 80:20 split between meeting the austerity agenda through a combination of service efficiencies and tax up-lifts, similar to central Government's strategy for addressing the national fiscal deficit. Sustaining this level of further savings year on year is becoming harder for services to deliver, making tracking of action plans to deliver efficiencies even more important.

1.8. Other significant risks in the new MTFP (2015-20) relate to:

- potential policy changes (including service specific and fiscal) following the General Election in May 2015;
- the potential for revisions to the basis of local government funding. A Commission into Local Government Funding jointly carried out by the Local Government Association (LGA) and CIPFA is expected to report early in 2015 and propose changes ahead of the next Comprehensive Spending Review. In addition, there are calls for wider pooling of health and social care funding; the increased devolution of responsibilities to local authorities; and, other changes to statutory responsibilities take effect (for example the Care Act). Finally, the trend towards increasing complexity in allocating funds: through bidding processes and match funding, rather than grant allocations, makes forecasting total funding available less predictable. All these challenges to forecasting the quantum of funding likely to be available and to the distribution mechanism, lead to increased uncertainty around the level of actual funding the Council will receive in the future; and
- the continuing increases in demand, both volume and complexity, for the core services that the Council has a duty to provide to vulnerable residents, in particular relating to children, schools places and the elderly, all increase the pressures to spend more on core services. This is particularly difficult to manage at the same time as the continuing reduction in funding levels, through loss of grant and restraint in council tax up-lifts as a result of the Governments council tax referendum policy.

1.9. In response to these pressures and uncertainties and mindful of the need to remain focused on long term financial resilience, the Council is planning deeper and earlier efficiencies to balance the budget for 2015/16 without erosion of the councils general reserves and balances. In addition, the Council proposes to continue with the strategy to remove the risk contingency from 2015/16, to avoid unnecessarily increasing the efficiencies required to be delivered.

1.10. However, to recognise the risk of non-delivery of efficiencies going forwards the additional mechanism to regularly track and monitor progress on the implementation of robust plans for achieving the efficiencies across the whole MTFP period, that was introduced in 2014/15, will continue to ensure early action can be taken if it emerges that any plans become non-deliverable. This mechanism specifically involves regular supportive budget challenge sessions led by the Chief Executive and the Director of Finance with the key Heads of

Service and Strategic Directors. Ahead of 2015/16 this mechanism has being expanded to supportive challenge of the key transformational initiatives (for example the family support programme and the transformation of emergency response services).

1.11. To balance the budget, the Council proposes a council tax up-lift of 1.99% for 2015/16, in the context of a referendum limit of 2%. This strategy is consistent with recent years whereby the up-lift has been below inflation whilst also recognising that freezing the council tax would erode the long term financial resilience of the Council. Looking ahead, the Council proposes to link council tax up-lifts to the current increases in uncontrollable service demands caused by demographic changes. However, the precise level of this cannot be determined until greater certainty is known once the new Government is formed after the General Election in May 2015.

1.12. For the last three years this has meant not accepting the Governments council tax freeze grant (CTFG) and instead putting in place sensible council tax up-lifts. For 2015/16 the Provisional Financial Settlement has indicated a fifth council tax freeze grant at 1% (for 2015/16). In the absence a Comprehensive Spending Review beyond 2015/16, it is not known whether this CTFG will be added to the council's case funding in the longer term.

1.13. Accepting this grant would be inconsistent with the Council's long term strategy and would erode the Council's funding base: particularly important to this Council because of the high dependence upon council tax funding as a result of low central Government grant support and high service demand pressures as a result of demographics.

Financial management arrangements

1.14. For 2013/14 the Council received another unqualified opinion on the Council's financial statements and an unqualified conclusion on the Council's arrangements for securing value for money. The Council was rated as 'good' (the top rating) in terms of its financial resilience.

1.15. The Director of Finance continued to work closely and positively with the council's external auditor, Grant Thornton.

1.16. The Council has continued its robust system of budget monitoring and control evidenced by the continuation of monthly budget monitoring reports to Cabinet within a month of the period end. Where over-spends or under-spends have arisen, prompt management actions have been identified to minimise effect and to enable early corrective action to be put in place where relevant.

1.17. The system for monitoring the progress on the implementation of efficiency savings has been enhanced during 2014/15, as requested by Cabinet and now includes supportive budget challenges sessions led by the Chief Executive and Director of Finance with the Strategic Directors and Heads of Services for the largest spending areas. Scrutiny by the Leader and Cabinet, as well as Council Overview Scrutiny Committee will continue as before.

1.18. The Director of Finance considers that the financial control arrangements remain sufficiently robust to maintain adequate and effective control of the budget in 2015/16.

Budget process

1.19. The budget planning process, established in 2011, following a 'lean' process review, was developed further for this MTFP (2015-20) process. The main enhancement was to establish closer challenge of the service strategies and action plans in place to ensure effective delivery of service efficiencies.

1.20. The budget has been constructed by looking at expected activity for the future years rather than the incremental approach. This applies a consistent approach to preparing budget proposals across all services. The assumptions, calculations and proposals in this budget are the result of challenge and scrutiny by the Leader of the Council, Members of the Cabinet and Select Committees throughout the summer and autumn of 2014 and into January 2015 guided by advice from the Chief Executive, Strategic Directors and Director of Finance.

MTFP (2015-20) budget assumptions

1.21. The main budget assumptions are set out in detail in the main budget report and the Director of Finance confirms that these are realistic in the context of the demographic and fiscal challenges facing the Council, although the proposed efficiency and other service savings are ambitious and there is substantial risk they will not all be achieved within the required timescale. This is why the enhanced tracking of action plans to deliver efficiencies will be continued and the MTFP reviewed in the summer 2015.

1.22. In recognition of the need to invest to deliver some of the efficiencies & service reductions required, the invest to save fund created in 2010/11, against which services will be required to produce full business cases before any resources are actually released, will continue in 2015/16. As in 2014/15, this reserve will require services to 'repay' the investment released to them over an agreed period – thereby ensuring that this fund is replenished over time and available for future investment initiatives.

Level of reserves and balances

1.23. The final accounts for 2013/14 show available general balances at 31 March 2014 of £21.3m. The latest budget monitoring position for 2014/15, as at 31 December 2014, forecasts that this level will be £21.3m by 31 March 2015. Appropriate levels of general balances are necessary to be maintained so that the Council can respond to unexpected emergencies. In recent years this balance has been set at between 2.0% and 2.5% of the sum of council tax plus settlement funding, i.e. £16m to £20m. Although the current expected level is marginally in excess of this, the Director of Finance considers this prudent in view of: the removal of the risk contingency from the revenue budget into

2015/16; the increasing uncertainty of specific grants; and, the absence of a specific reserve to manage severe weather liabilities.

1.24. Details of earmarked balances are set out in Appendix A7. After using significant earmarked reserves in the 2014/15 budget, and having reviewed the reasons for holding each balance, the Director of Finance considers it prudent to leave earmarked reserves at broadly the same level going into 2015/16: £95m. The minor changes proposed are:

- to use £4.3m of funds from the Budget Equalisation Reserve to smooth spending across financial years; and
- to add the excess Council Tax Collection Fund surplus (£4.6m) to the Economic Downturn Reserve.

1.25. Taking the general balances and the earmarked reserves together, the Director of Finance considers the amounts represent a prudent and sensible level for likely future commitments, whilst not holding excessive balances when services are facing increasing demands.

Financial standing

1.26. The Council has complied fully with the requirements of the Prudential Code for Capital Finance in Local Authorities. The formal recommendation to the Council sets out the prudential indicators, which the council must adhere to. In accordance with the planned capital programme, and the provision made in the current MTFP (2014-19), during the current financial year, 2014/15, the Council has borrowed £50m (in two tranches), at record low interest rates, thereby minimising the long term costs of repayment by the Council. Looking ahead into 2015/16, it may be that further borrowing will be undertaken ahead of forecast rises in interest rates later in the year. As the Council reviews the MTFP in the summer 2015, regard must be given the ensuring that the revenue costs of proposed borrowing are affordable and sustainable in the long term.

Risk assessment

1.27. In response to the significant challenges that the Council is facing and the associated emerging risks, an integrated risk framework comprising the separate disciplines of risk management is well established in the Council and will be maintained. This has seen several changes to the risk governance arrangements embedded in the Council and the close link between risk registers and business impact analyses and continuity plans has been sustained throughout 2014/15 and will continue into 2015/16. Similarly the Leadership Risk Register remains in place and will continue to be monitored monthly by the Chief Executive and senior officers, and reviewed by Cabinet quarterly in 2015/16.

1.28. The specific risks relating to the financial environment and opportunities facing the Council and recorded in the Leadership Risk Register are listed below and many lead to the proposal to review the MTFP (2015-20) in the summer 2015 once some of these are clearer:

- erosion of the council's main source of funding (council tax);
- delivery of the major change programmes and associated efficiencies;
- increased reliance on partnership working to manage service delivery and optimise efficient service delivery;
- the on-going uncontrollable growth in demographic demands on services;
- potential policy changes (including service specific and fiscal) following the General Election in May 2015; and
- the absence of a Comprehensive Spending Review 2015.

1.29. The Director of Finance is satisfied that the proposed budget, general balances & earmarked reserves sufficiently addresses these risks. Additional resilience has been assured over the long term through sustaining the earmarked reserve for long term Investment & Infrastructure initiatives, the continued use of the Budget Equalisation Reserve to enable spending to be smoothed across years, and the increase to the Economic Downturn Reserve in view of the on-going local government funding uncertainty.

Future years

1.30. The proposed budget addresses the estimated reduction in funding over the next five years and sets out a plan to ensure that the Council can deliver budgets within estimated available resources. The plan will require close monitoring and, in view of the increased uncertainty around Government funding, council tax and business rates, as well as on-going high demographic demand for core service, it is likely that adjustments will be required during 2015/16 to take account of unforeseen events and changes in the underlying assumptions. However, it sets a clear direction for the future and places the Council in a sensible position to meet the challenges ahead.

1.31. Given the scale of the financial challenges facing the public sector, the Director of Finance must emphasise the high likelihood that the next Comprehensive Spending Review (CSR) will introduce further government grant cuts, meaning any changes to services over the MTFP (2015-20) period must be sustainable in the long term. It ought to be recognised that the content of the next CSR is particularly hard to forecast in view of the General Election in May 2015.

Conclusion

1.32. The Director of Finance considers that the budget proposals recommended by the Cabinet are robust and sustainable. However, there are considerable risks associated with the increased uncertainty in a number of areas as set out above. This means a review of the whole MTFP (2015-20) period is recommended in the summer 2015 to validate assumptions and timescales.