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 Section 151 Officer 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. For Surrey County Council the Section 151 Officer is the Director of Finance, Sheila Little.

1.3. The Council is required to set a balanced budget and in considering the budget, the Council must have due regard to the advice the Director of Finance includes in this report. The following paragraphs therefore provide a commentary on the robustness of the budget and the reserves in place to support the Council.

1.4. 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.

1.5. Strategically the financial and economic context facing the Council remains similar to recent years, which is a continuation of austerity and significant, and very unexpected, reduction in central Government funding. The Government made their Provisional Settlement on 17 December 2015 and the Council learnt that it faces a 42% reduction of core central Government funding when compared to the current year. The Council had, in accordance with what could be reasonably assumed from previous Government indications, been planning for a reduction of 28% into 2016/17. The difference in the figures compared to those that could reasonably be expected, reflect that the Government made changes to the basis of distribution of their core funding (Revenue Support Grant) for which that had been no previous indications and or consultation.

1.6. At the same time, the Council faces significant pressures from the care market as well as increasing year on year demographic demand for services, in particular, but not exclusively, for social care. Public expectation about, for example, the Highways service is also increasing. The Government has announced a four year settlement for core funding, which provides some certainty over Government funding in future years. However, at the time of writing this report, the council has not received notification of the level of government grants for £128m (15%) of its services. This increases the level of uncertainty and the council may need to draw on reserves if the allocated amounts vary from those planned for.

1.7. As well as confirming the general Council Tax precept limit, without referendum at 2%, as expected, the Government has recognised the increasing social care pressures, and are allowing authorities with adult social care responsibilities the ability to increase Council Tax by an additional 2% without a referendum requirement. Authorities must provide assurance that this funding will be used for adult social care services. This additional precept would raise £11.8m for the Council, although this is less than the demographic demand for adult services which increases by over £20m each year. In addition to these demographic demands, there are further significant inflation and price pressures facing the service from the care market, not least of all due to the recently introduced National Living Wage. These total £11m for 2016/17 alone.

1.8. To help the Council manage these demand pressures, the Cabinet is proposing that the Council continue with its existing Council tax strategy of raising Council Tax by a general 1.99%, as currently planned in the MTFP (2015-20) and the additional 2% for adult social care. This means an increase in Council Tax of 3.99% for 2016/17 (raising £31m) and for each of the following four years of the new MTFP period (2016-21).

1.9. Even with the planned increases in Council Tax and the existing efficiencies and savings plan, the Council cannot continue services as they currently are and produce a long term sustainable budget. Although the additional adult social care precept is a late and largely unexpected help (£11.8m), other significant unexpected and late funding reductions announced in the Provisional Settlement more than off-set the gain from the adult social care precept. To explain, amended distribution methodology for allocation of RSG will mean £47m less funding from 1 April 2016, £20m of which the Council could not reasonably have forecast. Also, total service pressures of £71m and inflation pressure of £26m add further to the challenge.

1.10. The position for future years worsens as continual efficiencies become harder to sustain and realise and yet demographic pressures continue to escalate and government funding reduces further and faster than could reasonably have been expected. Unlike previous changes to local government funding, the government has not proposed any damping mechanism.

1.11. Together this means the Council must continue to explore different ways of delivering services and proposes to establish a significant transformation programme early in 2016 to identify service changes that reduce costs and provide income generation opportunities.

1.12. However, the late notification means the Council is only able to balance the budget for 2016/17 and 2017/18 by a combination of the following:

- limiting spending in the current financial year, 2015/16, to ‘essential’ spend only;
- requiring deeper and earlier efficiencies from services (£18m making a total for 2016/17 of £84m);

- amending its council tax strategy to a general council tax increase of 1.99% and to implement the additional precept introduced to help fund adult social care services of 2%; making a total Council tax increase of 3.99% in 2016/17 and each of the subsequent four years of the MTFP period;
- utilising a significant proportion of its reserves (£17.2m, 19% in 2016/17);
- making use of up to £30m of capital receipts from asset sales to fund a significant transformation programme, and;
- assuming that the Government will allocate transitional relief to compensate the Council for the 'shock' element of the redistribution mechanism through damping in the Final Settlement.

1.13. It is important to recognise that the Council has successfully delivered significant efficiency savings & service reductions in each of the last five financial years (£331m), and is forecast to deliver further savings for 2015/16 of £67m. A further £384m savings are planned for the next five year MTFP period although it is recognized that this is increasingly challenging to deliver year on year.

1.14. To recognise the risk of non-delivery of efficiencies going forwards and the risks inherent in the budget assumptions set out above, a number of mechanisms are in place to help manage these risks, including:

- monthly reporting to Cabinet on budget monitoring forecasts within 3 weeks of the period end and including remedial management action where required;
- the operation of a robust risk management approach;
- the presence of the council's key internal control framework, including the financial regulations and Scheme of Delegation for Financial Management which provides the framework for delegated budget management;
- the sustaining of good working relations with the external auditor (Grant Thornton);
- the operation of the internal audit function and its role in assessing controls and processes to highlight any major weaknesses and advise on best practice, and;
- the continuation of the of supportive budget challenge sessions led by the Chief Executive and the Director of Finance with the key Heads of Service and Strategic Directors

1.15. However, the situation is very serious. The above measures will not eliminate the risks entirely and will not on their own ensure the Council can deliver a balanced budget in future. Therefore, it is proposed to introduce a significant Public Value Transformation programme led by the Chief Executive and the Director of Finance to ensure that significant service delivery changes are planned and delivered to ensure that the budget the Council sets is sustainable. The inevitable time needed to plan these changes thoroughly and to consult properly makes the provision of transitional relief by Government essential for the Council to set a sustainable budget.

Level of reserves and balances

1.16. The final accounts for 2014/15 show available general balances at 31 March 2015 of £21.3m. The latest budget monitoring position for 2015/16, as at 31 December 2015, forecasts that this level will be maintained at £21.3m by 31 March 2016. 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 recent significant unexpected variations in the level of Government funding as well as the on-going uncertainty in the level of specific grants (revenue and capital); and, the absence of a specific reserve to manage severe weather liabilities.

1.17. Details of earmarked reserves are set out in Appendix A7. The extra reduction in RSG funding announced in the Provisional Settlement will require the use of significant reserves to support the budget over the next two years. The Council will need to consider the extent to which these reserves need replacing in the medium term, whilst not seeking to holding excessive balances when services are facing increasing demands.

Financial standing

1.18. 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, to which the council must adhere. In accordance with the planned capital programme, and the provision made in the current MTFP (2015-20), during the previous financial year (2014/15), the Council forward borrowed £90m in respect of the 2015/16 year in three £30m tranches (16 February 2015, 27 February 2015 and 19 March 2015), at record low interest rates, thereby minimising the long term costs of repayment by the Council. Looking ahead into 2016/17, it may be that further borrowing will be undertaken ahead of forecast rises in interest rates later in the year, paying due regard to ensuring that the revenue costs of proposed borrowing are affordable and sustainable in the long term.

Risk assessment

1.19. In response to the significant challenges that the Council is facing and the associated emerging risks, an integrated risk framework is well established across the Council and will be maintained. The risk governance arrangements are well embedded and the close link between risk registers and business impact analyses and continuity plans has been sustained throughout 2015/16 and will continue into 2016/17. 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 and Audit and Governance Committee quarterly in 2016/17.

1.20. The specific risks relating to the financial environment and opportunities facing the Council and recorded in the Leadership Risk Register are listed below:

- constraints in the ability to raise local funding and/or distribution of funding;
- increased reliance on integrated working and implementing new models of delivery to manage service delivery and optimise efficient service delivery;
- the on-going uncontrollable growth in demographic demands on services.

Conclusion

1.21. Although the level of risk remains significant and the position is very serious, taking all of the above into account, it is the view of the Director of Finance that the budget proposals recommended by the Cabinet will produce a balanced budget for 2016/17 that is deliverable, and develop a longer term budget that is sustainable so long as:

- Government provides transitional relief in the Final Settlement,
- All existing savings plans are delivered in full, and;
- that the Public Value Transformation programme is adopted, managed and monitored rigorously by the Chief Executive and Director of Finance to ensure it identifies considerable base budget reductions in costs and income generation opportunities as soon as is manageable.

This page is intentionally left blank