Deputy Leader

Decision to be taken on or after 17 August 2018

Local Authority Financial Resilience Index – Responding to the Chartered Institute of Public Finance & Accountancy's Consultation

Recommendations

The Portfolio Holder is asked to:

1) Agree the County Council's draft response to the consultation paper as set out in **Appendix A**.

2) Delegate authority to the Strategic Director for Resources and the Head of Finance to approve any further adjustments to the consultation response prior to the submission date of 24 August 2018, providing they are consistent with the proposed responses in this report.

1. Background

1.1. The Chartered Institute of Public Finance and Accountancy (CIPFA) recently released a consultation on its plans to launch an authoritative measure of local authority financial resilience through the creation of a new local authority financial resilience index.

1.2. CIPFA is proposing to use a range of indicators for the index, including the rate of depletion of reserves, level of reserves, demographic and social services pressures and level of borrowing.

1.3. CIPFA is working with local authorities to decide how the index should work and what criteria should be included and to do so is consulting widely. This report seeks approval for our response as part of this consultation process. The six criteria proposed for inclusion in the index are:

- The level of total reserves, excluding schools and public health, as a proportion of net revenue expenditure.

- The percentage change in reserves, excluding schools and public health, over the past three years.

- The ratio of government grants to net revenue expenditure.

- Proportion of net revenue expenditure accounted for by children's social care, adult social care and debt interest payments.

- Ofsted's overall rating for children's social care.

- Auditor's VFM judgement.

1.4. After the consultation period, which closes on 24 August 2018, CIPFA expects to produce the first edition of the resilience index in the early autumn this year.

2. Key Issues

2.1. CIPFA is right to acknowledge the need for public accountability and the fiduciary duty to the taxpayer. Failure to take appropriate financial action has a direct and often negative impact on local people and also the sector itself. However, all local authorities have a responsibility to ensure that the design, production, presentation and interpretation of financial data cannot be easily misinterpreted or misused, as this can also negatively impact on both the sector and local people. In responding to the consultation we must ensure that any index that is implemented supports the political leadership, senior managers and the Section 151 Officer to improve financial management and accountability and has a net benefit for tax payers.

2.2. Recent failings at other local authorities have brought a lot of attention to local government, in particular to shire counties. There were clearly systemic issues at these local authorities but these issues do not necessarily apply to the whole sector. It is therefore important that an index does not simply provide central government and critics with undue 'evidence' of perceived wider financial management shortcomings that detract from the funding challenges all local authorities are facing. This would also be inconsistent with the need for public accountability and the fiduciary duty to the taxpayer. If an assessment of financial resilience is presented appropriately, it could be a helpful tool for the authority.

2.3. The well-publicised reports into the failings of other authorities have shown that the problems run deeper than mere financial measurements. Even if CIPFA are able to balance this piece of work in a fair way, it doesn't necessarily mean an authority will act on it. It is also important that any index is set within a wider context of the whole raft of tools that are available to support officers and members in ensuring proper financial management in an authority. It is likely that an authority that is properly run and has an appropriate culture will already be aware of its financial position, and this index will merely confirm that view.

2.4. The draft response to the consultation is attached at **Appendix A** and reflects these issues. The Deputy Leader is asked to approve the response to the consultation and delegate authority to the Strategic Director for Resources and the Head of Finance to finalise the response prior to its submission on 24 August 2018 providing it is consistent with the points raised in this draft response.

3. Background Papers

3.1. None.

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The following Elected Members have been consulted on this report prior to its publication:

Cllr Izzi Seccombe, Cllr Peter Butlin, Cllr Parminder Singh Birdi , Cllr Sarah Boad, Cllr Maggie O'Rourke, Cllr Heather Timms

Appendix A

DRAFT Consultation Response

General Comments

CIPFA is right to acknowledge the need for public accountability and the fiduciary duty to the taxpayer. Failure to take appropriate financial action has a direct and often negative impact on local citizens and also the sector itself. However, all local authorities have a responsibility to ensure that the design, production, presentation and interpretation of financial data cannot be easily misinterpreted or misused, as this can also negatively impact on both the sector and local citizens. Any index that is implemented must support the political leadership, senior managers and the Section 151 Officer to improve financial management and accountability in their authority and have a net benefit for tax payers.

Recent failings at other local authorities have brought a lot of attention to local government, in particular to shire counties. There were clearly systemic issues at these local authorities but these issues do not necessarily apply to the whole sector. It is therefore important that an index does not simply provide central government and critics with undue ‘evidence’ of perceived wider financial management shortcomings that detract from the funding challenges we all face. This would also be inconsistent with the need for public accountability and the fiduciary duty to the taxpayer. If a measure of financial resilience is presented appropriately, it could be a helpful tool for the authority.

Technical Response

Set out below are specific comments on the proposed indicators, along with some suggested changes:

- Indicator 1 - The level of total reserves excluding schools and public health as a proportion of net revenue expenditure.

It is not clear from the documentation if this is a measure of all reserves or if it excludes earmarked reserves. Clearly in a crisis, an authority may well turn to all reserves, not just non-earmarked. However, we believe this measure should only relate to non-earmarked. We are not clear why Public Health reserves are excluded

– given the direction of travel of this source of funding, the exclusion of Public Health reserves is not relevant.

- Indicator 2 - The percentage change in reserves, excluding schools and public health, over the past three years.

The same comment regarding Public Health reserves applies. In addition, we note the comment 'If a council is reducing its reserves it may not be achieving necessary savings to balance its budget.' Whilst this may be correct, it could also be the case that authorities are withdrawing reserves to use them for the purpose for which they are intended. It is important that the local context is taken into account.

It may be worth exploring the unintended use of reserves – this could be investigated by reference to reserves being used when the budget is set, compared to reserves being used at outturn – a difference would be worth investigating as it may be that savings incorporated as part of the budget were not being delivered.

- Indicator 3 - The ratio of government grants to net revenue expenditure.

The third suggested indicator 'the ratio of government grants to net revenue expenditure' seems almost irrelevant, given the fact that both public health and Revenue Support Grant will be ending. We don't believe this adds value to a resilience index. We also don't believe that any indicator which measures individual funding streams (eg. Council tax, business rates etc.) is useful – it is the composite amount compared to expenditure which is important. And to that extent, we suggest a measure of gross expenditure to council tax, business rates, specific grants and fees and charges is applied – difference will show the extent to which reserves are used to set the budget. If this is used in the context of a trend analysis, it will be possible to see a reliance on reserves to balance the budget.

- Indicator 4 - Proportion of net revenue expenditure accounted for by children's social care, adult social care and debt interest payments.

The fourth suggested indicator measures the proportion of adults and children's social care to net expenditure. This does have a fundamental flaw. If net expenditure is greater than sustainable funding streams (i.e. the budget has been balanced by use of reserves), then measuring the proportion of social care and debt spend to expenditure could be understating a structural problem in the budget. We therefore suggest this is compared to recurrent funding streams. In addition, as a pressing issue, we also suggest the inclusion of Special Educational spending given it is the root cause of other pressures and volatility such as home to school transport spending.

- Indicator 5 - Ofsted overall rating for children's social care.

History has shown that any authority that has an ‘inadequate’ or ‘requires improvement’ rating is likely to have to invest substantial sums in improvement programmes. The difficulty is that the extent of additional investment required and the period for that investment can vary significantly due to the actual rating and the action required, there is therefore a question on whether there should be a differential in scoring depending on the detail of the rating across all the classes. However, this may make this measure too complex and cumbersome.

- Indicator 6 - Auditor’s VFM judgement.

For this indicator to be meaningful we believe there should be a greater definition of the assessment and guidance to ensure consistency in the assessment – we do not believe this is the case at the moment. The amount of time the external auditor spends on this measure is low and given this is weighted as providing 10% of the overall total, it is important that there is confidence in its consistent application.

Further Comments

We believe that using a RAG system and a combined weighting system is overly simplistic and could potentially distract from the message. As an alternative, if each measure was given an individual score and this detail is published, then it would provide more meaningful and informative information. The index would then become a more useful tool for s151 officers and leaders, sitting alongside others such as the CFO insights, to help inform and guide financial management and planning in the local authority in a targeted way. Therefore, we support the position of the Society of County Treasurers that a “balanced scorecard” type approach would be more appropriate and enable more pertinent comparisons to be made, which would allow each authority to target its actions where they are most needed.

We are also concerned that the system is a relative one. An authority’s score or scores can only be measured in relation to others in the same group (e.g. all County Councils). If the financial situation of the whole group is serious (as is the case at the moment given the state of local authority funding), then a ‘green’ rating for an authority merely means it is more resilient than others not that is its resilient per se. In this scenario, it therefore provides a degree of confidence which may mislead.

Further work may be needed on this to provide an appropriate benchmark, for example, what is the minimum level of finance required for any specific authority given the particular services they provide.

Recent events have shown that the problems with authority’s finances run deeper than mere financial measurements even if CIPFA are able to balance this piece of work in a fair way, it doesn't necessarily mean an authority will act on it. The proposed 'code of Financial Management' currently in development might be a more appropriate place to judge how an authority deals with criticism, and therefore, a more effective way for councils to maintain, and be seen to maintain, a grip of their budgets.

We also feel it is important that this index is set within a wider context of the whole raft of tools that are available to support officers and members in ensuring proper financial management in an authority. It is likely that an authority that is properly run and has an appropriate culture will already be aware of its financial position, and this index will merely confirm that view. What is needed, is that an authority where there is less acknowledgement of its position takes this messaging on board.

The above points exemplify Warwickshire County Council's wider concerns. The implementation of such a system must be fair, not be able to be misconstrued and have both relevant indices and accurate weightings. We urge CIPFA to take more time in developing the system, or potentially look at alternatives, including considering what other information is available at local level (such as delivery of savings). It may be appropriate to consider collection of this local data to build a wider dataset.