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Financial Resilience Assessment

Caerphilly County Borough Council

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Status of report

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The team who delivered the work comprised Sara-Jane Byrne and Janet Smith.

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Summary report

Summary

1. Good financial management is essential for the effective stewardship of public money and the delivery of efficient public services. Good financial management:
   - helps authorities take the right decisions for the short, medium and long term;
   - helps authorities deliver services to meet statutory obligations and the needs of local communities;
   - is essential for good corporate governance;
   - is about managing performance and achieving strategic objectives as much as it is about managing money;
   - underpins service quality and improvement;
   - is the basis of accountability to stakeholders for the stewardship and use of resources; and
   - is a key management discipline.
2. Long-term financial management is not about predicting the future; it is about preparing for it. Authorities need to understand future demand, assess the impact of probable changes, review the gap between funding needs and possible income, and develop appropriate savings strategies.
3. Well-considered and detailed long-term financial strategies and medium-term financial plans can ensure the delivery of strategic priorities by enabling appropriate financial choices. Conversely, short-term annual budget planning alone encourages an incremental and process-driven approach that can be ineffective in a period of rapid external change.
4. Financial resilience is achieved when an authority has robust systems and processes to effectively manage its financial risks and opportunities, and to secure a stable financial position.
5. Our April 2015 report 'The financial resilience of councils in Wales' was based on fieldwork carried out in all Welsh local authorities. From this work, and from other available material related to aspects of financial management, we have drawn together some key characteristics of good practice to assist practitioners in developing their arrangements. These characteristics can be found at Appendix 1.
6. Given the continuing pressures on funding, we have considered whether the authority has appropriate arrangements to plan to secure and maintain its financial resilience in the medium term (typically three to five years ahead). While there may be more certainty for the authority over an annual cycle, financial pressures impact beyond the current settlement period. We have considered evidence of the authority's approach to managing its finances in the recent past and over the medium term when reaching our view on the authority's financial resilience.
7. We undertook our assessment during the period May to December 2015, and followed up issues highlighted in the 2014-15 financial position work. The focus of the work was on delivery of 2014-15 savings plans, and the 2015-16 financial planning period.

8. The work focused on answering the following question: **Is Caerphilly County Borough Council managing budget reductions effectively to ensure financial resilience?** In this report we also consider whether:

- **financial planning arrangements effectively support financial resilience;**
- **financial control effectively supports financial resilience; and**
- **financial governance effectively supports financial resilience.**

9. Overall, we concluded that the Council has effective financial control arrangements and a track record of achieving savings in advance. However, it does not have a comprehensive medium term financial plan and monitoring progress of savings is fragmented. We came to this conclusion based on our findings in relation to financial planning, financial control, and financial governance arrangements.

10. This report gives a risk rating for each aspect: financial planning, financial control and financial governance. The descriptors for risk ratings are set out below:

Low risk	Arrangements are adequate (or better) with few shortcomings in systems, processes or information. Impact on the authority's ability to deliver its financial plan may be minimal.
Medium risk	There are some shortcomings in systems, processes or information that may affect the authority's ability to deliver the desired outcomes of its financial plan.
High risk	There are significant shortcomings in systems, processes or information and/or there is a real risk of the authority's financial plan not delivering the desired outcomes.

11. We rate the risk to the Council's delivery of its financial plan for each of these elements as follows:

Medium Risk	Financial planning
Low Risk	Financial control
Low Risk	Financial governance

Proposal for improvement

P1	The Council should strengthen its financial resilience by: • developing more explicit links between the Medium Term Financial Plan (MTFP) and its corporate priorities; • developing a longer term MTFP with comprehensive multi-year savings plans to cover the period of the MTFP; • continuing to develop a more strategic asset management plan which is aligned to its MTFP; • reporting 'Whole Council' financial and savings progress reports to Members on a regular basis; and • developing income generation/charging policies.

The Council has effective financial control arrangements and a track record of achieving savings in advance. However, it does not have a comprehensive medium term financial plan and monitoring progress of savings is fragmented

Financial Planning

The Council has a track record of operating within its budget, but its medium term financial plan and supporting savings plans for future years need to be more fully developed

12. The Council has a corporate framework in place for financial planning. The Council engages well with Members, including holding seminars and special scrutiny committees during the autumn and winter each year to discuss budget and savings proposals prior to formal consideration of the budget in February.

13. The Council has a corporate plan together with identified improvement objectives. In our financial resilience report issued to the Council in May 2015, we identified that the Council should ensure that it explicitly considers its priorities and improvement objectives when determining its savings plans. However, the extent to which the Council's priorities and improvement objectives have influenced the Council's Medium Term Financial Plan (MTFP) is still not clear. We understand from officers that the Council's priorities do informally influence the MTFP but this consideration is not explicit.

14. Service plans demonstrate links to the Council's MTFP and the MTFP highlights key service pressures. Service managers are proactively engaged in identifying savings proposals.

15. The MTFP is supported by appropriate human resource related policies, such as redeployment, flexible retirement and redundancy policies.

16. The Council's financial planning process takes account of its asset base. The Council's MTFP includes asset-based savings, such as the closure of its office in Pontllanfraith. However, the Council does not have an agreed strategic asset management plan, which is aligned to the MTFP. The Council is in the process of using its Asset Management (Land and Property) strategy as a framework to develop a more comprehensive and robust asset management strategy.

17. The Council has a track record of delivering a surplus on its budget. The Council exceeded its planned budget outturn for 2014-15 by £10.9 million with underspends across service directorates of approximately £6.6 million. There have been some recurring large underspends in some budgets, which the Council has now realigned.

The Council reported underspends transparently to its Scrutiny Committees throughout the year, identifying those which were likely to contribute to future savings plans.

18. The Council approved its MTFP 2015-2018 in February 2015 and revised it in September 2015. In February 2015, the Council identified a budget shortfall of £12.8 million for 2015-16, a further £14 million for 2016-17 and £12.1 million for 2017-18. The Council updated its MTFP in October 2015 and rolled it forward to cover the period 2016-17 to 2018-19. The Council assumed a worst-case scenario of reductions in funding of 4.3 per cent for 2016-17 and 2017-18, and three per cent for 2018-19. Revised savings proposals amounted to £14.3 million for 2016-17, £11.4 million for 2017-18 and £9.4 million for 2018-19.

19. The Council's prudent approach to its finances in the past has enabled it to take a forward-looking approach to identifying its savings requirements. It has achieved some savings in advance, with minimal planned savings not being delivered in-year or carried forward. Budgets have been set taking into account the level of savings already identified and achieved in prior years.

20. In 2015-16, the Council undertook a systematic review of base budgets, resulting in identification of budget reductions for 2016-17. The majority of savings plans for 2015-16 and 2016-17 included 'global proposals' for each directorate relating to vacancy management, budget realignment, service structure reviews and minor changes in service provision with no impact on front line services. This is in line with the Council's desire to protect front line services in so far as possible. These savings proposals are subject to review by the Corporate Management Team. Challenge sessions with individual Heads of Service, relevant directors, Interim Head of Corporate Finance and the Finance Manager for the relevant service area also take place. The Council feels this process has facilitated ownership, accountability and scrutiny of savings proposals.

21. The Council identifies the remaining discrete savings proposals individually. Savings proposals include the amount, description, risk of impact on the service user/public and status of support for proposals following the budget consultation process.

22. Reasonable assumptions around, for example, inflation, income levels, demographics, and future demand for services, underpin the Council's MTFP. However, the projected budget shortfalls for 2016-17 to 2017-18 were high level and there was limited evidence of scenario planning to assess the impact in funding changes. In the main, the same estimated amounts were used for key variables such as budget pressures and demographic changes as those used in the 2015-16 budget.

23. The Council has identified indicative savings for future years. The Council has planned the delivery of some larger scale future savings proposals, such as the closure of Tŷ Pontllanfraith in February 2015 to achieve savings in 2016-17. However, aside from this, the MTFP did not include detailed and costed savings plans for future years. In effect, the 2015-16 to 2017-18 MTFP focussed heavily on the 2015-16 annual budget and did not constitute a detailed MTFP.

24. Moreover, the Council's focus on achieving savings through global proposals such as vacancy management and budget realignment is not sustainable given the scale of savings required in future years. The Council would benefit from a longer-term financial strategy, which provides greater detail about how it will address its budget shortfall over the term of the strategy. This may require the Council to identify savings which are of a more strategic and transformational nature.

25. The Council recognises that it has to change the way it runs services to meet the financial challenges ahead. The Council has agreed the following five principles, which will be taken into account in the identification of its savings proposals:

- protecting front-line services where it can and reducing expenditure on management and administrative costs;
- increasing fees and charges where appropriate;
- reducing, rather than removing, services where possible;
- focussing on priorities; and
- looking at alternative ways of delivering services (collaboration, partnerships, community trusts, etc).

26. In consultation with appropriate Cabinet Members, the Corporate Management Team has led the work to identify savings proposals following these five principles.

27. Following the Comprehensive Spending Review in autumn 2015, the Council was informed that it will receive a more positive Revenue Support Grant settlement from the Welsh Government than the Council had anticipated. The Council is now reprofiling the levels of savings needed to reflect this. It is now forecasting a budget shortfall of approximately £36 million over five years rather than nearly £39 million over three years. The Council is also revising its Medium Term Financial Plan to reflect this.

28. The Council's financial position is now such that it is able to take a considered approach to how it will address its budget shortfall over the medium term. It is positive that the Council is now taking the opportunity to develop a five-year financial plan.

29. The Council held a members' seminar on the revised MTFP in January 2016 and the Council agreed the 2016-17 budget and MTFP in February 2016.

Financial control

The Council's financial control arrangements are generally effective

30. The Council has a clear framework for managing the Council's financial affairs. The Council's constitution sets out the policies on financial and budget management, which define the roles and responsibilities of Members and Officers.

31. Budget reporting and monitoring take place at a number of levels within the Council and continue to be sound. Cabinet receives regular updates on the MTFP. Scrutiny Committees receive quarterly service budget monitoring reports, which highlight and explain any significant under and overspends, and identify potential cost pressures. Corporate Management Team routinely discusses 'hot spot' reports highlighting specific concerns or areas of budgetary pressure. Departmental management teams also discuss budget performance. Service budget monitoring reports include a section on the achievement of savings, focusing on those that are at risk of not being achieved.

32. The Council reviews and reports on its useable reserves annually. The Council have determined in recent years following the advice of the Section 151 officer to keep the Council Fund balance at or above a minimum agreed level of approximately £10 million. The Council is developing a Reserves Strategy, which will be considered by the Policy and Resources Scrutiny Committee in October 2016 prior to endorsement by Cabinet or Council. Officers provided a report to the Policy and Resources Scrutiny committee in April 2015 detailing the Council's useable reserves. The report set out the different types of useable reserves held by the Council. It also outlined the useable reserves relevant to each directorate. In the final accounts for 2014-15, the Council fund balance was £14.6 million as at 31 March 2015 and Council fund earmarked usable reserves were £60 million.Where the Council Fund is above £10 million at Outturn, monies are then transferred to one off initiatives.These are normally detailed in the budget report presented to Council in February. Historically, the Council has not used its reserves to balance its budget.

33. The Council does not use any explicit key performance indicators to monitor the MTFP and associated performance. The Council does not report and monitor key financial comparators for current, past and future years. Examples of such indicators used by other councils include working capital, gearing ratio and the reserves position. The Council does not formally benchmark its financial performance with other councils. The Council's Section 151 Officer does meet regularly with counterparts in other authorities.

34. The Council does not have an overarching policy on income generation/charging but it reviews fees and charges annually as part of the budget setting process. We understand that the budget consultation process highlighted that the public did not generally support increasing fees and charges. The Council is awaiting the outcome of our Local Government study on income generation and charging. It plans to use this to develop a corporate income generation/charging policy for 2016-17.

35. Internal and External Audit have not identified any significant weaknesses in the financial systems/processes, and internal controls are considered adequate.

Financial governance

The Council's financial governance arrangements are generally sound but there is a lack of regular whole-Council savings monitoring reports to members

36. The Council's Corporate Management Team clearly grasps the financial climate and the challenges the Council faces. Those responsible for managing financial performance are held to account at an individual and departmental level and by Members through the scrutiny process.

37. The Council's Section 151 Officer provides briefings and Budget Strategy Updates to directors and members on the financial challenges facing the Council.

38. The Council carried out public consultation on the 2015-16 budget and it amended or withdrew some savings proposals because of the feedback received. The Council has recently consulted the public, partners, voluntary sector, trades unions and members on its proposed savings plans for 2016-17. Through this, it has also made the public aware of potential areas for savings in 2017-18.

39. In our Financial Position Assessment report for 2014[1], we recommended, 'the Council should continue to implement a framework to formally monitor the deliverability of savings and report to Members'. Whilst the Council reports the achievement of savings on an exceptions basis for individual services to scrutiny committees, reporting arrangements are fragmented. A framework is not in place for regularly monitoring or reporting the achievement of savings targets on a 'Whole Council' basis. The Council does not report financial and performance information together.

40. The Council does not produce a savings monitoring report for the year-end and the 2014-15 revenue outturn report does not refer to the status of savings. The position against individual savings plans is not explicit and transparent. Therefore, whilst the 2014-15 quarter-three service monitoring reports forecast that the majority of savings would be achieved, it is not explicit if there were any service-specific undelivered savings from 2014-15 that have been carried forward to 2015-16. 'Whole Council' in year budget monitoring reports are not reported to Cabinet or routinely presented to the Policy and Resources scrutiny committee. For example, in 2014-15, only one report was presented. This does not allow for whole-service analysis or a whole authority view of the financial position of the Council at periodic points in the year. We understand that officers do monitor the overall position and would quickly report if the whole authority budget were not on track. However, our view remains that there is scope to strengthen the explicit monitoring of savings.

41. Until recently, the Council had an Improving Governance Programme Board in place, following two Reports in the Public Interest, which raised significant concerns about governance. The Council has recently disbanded the Improving Governance Board as it considers it has addressed the majority of actions. The Council also has a Corporate Governance Panel, which reviews its governance arrangements and co-ordinates the production of the Council's Annual Governance Statement.

42. The Council's Annual Governance Statement for 2014-15[2] identified the Council's scrutiny arrangements as an area for improvement. The Council agreed a series of changes to its scrutiny arrangements in October 2015. An action plan is in place to implement the changes. The Annual Governance Statement did not raise any significant issues relating to the Council's financial arrangements.

43. The Council's financial position is such that it has not needed to consider any radical or transformational changes to the way it delivers its services in order to balance its budget. Therefore, it does not have specific overview or programme boards in place to

[1] Details of our 2014 financial resilience report to be inserted.
[2] The 2014-15 Annual Governance Statement is available on the Council's website.

oversee and monitor the implementation of any change programmes. Recognising that the Council needs to adapt, the Corporate Management Team has developed a more structured approach to identifying and monitoring business improvement projects. This has entailed the creation of an Improvement Board consisting of the Corporate Management Team, a lead Cabinet Member and the Head of Service for Improvement. The Director for Community Services oversees the Improvement Board. A project manager supports the Improvement Board. This approach has been discussed and agreed by members.

Appendix 1

Key characteristics

Key characteristics of good financial planning
The authority's budget is set in the context of a longer-term financial strategy and a medium-term financial plan covering a three to five-year horizon.
The authority has clearly identified the savings it intends to make over a three to five-year term. The savings plan is underpinned by detailed costings and delivery plans for individual savings (including transformation/change savings).
The authority has a good track record of delivering on its savings plans.
Medium-term financial planning and annual budgeting reflect the authority's strategic objectives and priorities for the year, and over the longer term.
Assumptions around inflation, income levels, demographics, future demand for services and the costs of delivering services are modelled and based on reasonable predictions.
The authority understands its sources of income and the risks arising from these, and has reviewed its approach to fees and charges to ensure it achieves value for money.
Financial and corporate planning processes are integrated, link to risk management arrangements, and incorporate strategic planning for other resources including the capital programme and workforce planning.
The authority uses financial modelling to assess likely impacts on financial plans and required savings for different scenarios, and to help ensure short-term fixes are not achieved at the expense of long-term sustainability.
The authority models key expenditure drivers (for example, population changes and demand for services), sources of income (for example, income and government grant forecasts), revenue consequences of capital and resource requirements and balances.
The authority operates within a level of reserves and balances (including earmarked reserves and the general fund balance), approved by members, and appropriate to the strategic, operational and financial risks it faces.
If the authority is not at its target level for balances, there is planned action in place to achieve this, taking account of any associated risks to the organisation's financial position and delivery of its priorities.

Key characteristics of good financial control
The authority has an appropriate and effective budget management policy that clearly sets out roles, responsibilities and accountability. The scheme of delegation is clear, and processes are set out to manage budget under and overspends.
Financial monitoring and forecasting is fit for purpose and accruals based, helping to ensure a clear link between the budget, in-year forecasts and year-end position.
The authority analyses and extrapolates relevant trends, and considers their impact on the projected final out-turn.
The authority takes timely action to address any budget pressures, for example, by taking corrective action to manage unfavourable variances or by revisiting corporate priorities.
The authority has a good recent record of operating within its budget with no significant overspends.
The authority has agreed a clear policy on the use of its reserves. There is a clearly justified minimum level for its 'general fund' reserves balance. There is a clear rationale to explain transfer from, or between, reserves. Clear protocols explain how and when each reserve should be used. Decisions about reserves are underpinned by a comprehensive assessment of risk and current performance.
The reserves policy has been agreed by members and is subject to scrutiny.
The authority has a clear policy on income generation/charging. There is a register of charges across its services to help manage charges consistently. The authority has corporate guidelines on how concessions should be applied. Charges are regularly reviewed and the policy updated.
The authority monitors its key financial ratios, benchmarks them against similar bodies and takes action as appropriate.
The annual governance statement gives a true reflection of the authority.

Key characteristics of good financial governance
The leadership team clearly understands the significant and rapidly changing financial management challenges and risks facing the organisation, and is taking appropriate action to secure a stable financial position.
The authority has sufficient capacity and capability to promote and deliver good financial management.
The leadership team fosters an environment where there is good understanding and routine challenge of financial assumptions and performance, and a culture of transparency about the financial position.
The leadership team provides constructive scrutiny and challenge on financial matters to ensure arrangements remain robust and fit for purpose.
There is regular and transparent reporting to members. Reports include detail of action planning and variance analysis.
Members scrutinise and challenge financial performance effectively, holding officers to account.
Internal and external audit recommendations are dealt with effectively and in a timely manner.
There is effective engagement with stakeholders on budget issues, including public consultations.

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