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North Hertfordshire District Council

Review of the Council's arrangements for securing financial resilience

November 2011

Contents

Section 1

Executive summary

Introduction

Context

The Chancellor of the Exchequer announced the 2010 Spending Review (SR10) to Parliament on 20 October 2010. This formed a central part of the Coalition Government's response to reducing the national deficit, with the intention to bring public finances back into balance during 2014/15.

The associated report published Government Departmental Expenditure Limits (DELs) for the four-year spending review period: 2011/12 to 2014/15. Communities and Local Government (CLG) funding was reduced by 26% over the period.

SR10 represented the largest reductions in public spending since the 1920's. Revenue funding to local government will 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 have been frontloaded, with 8% cash reductions in 2011/12.

The provisional Local Government Finance Settlement was announced on 13 December 2010. The final figures were announced on 31st January with the debate and approval by the House of Commons on 9th February. This represents a two year funding announcement, because the Government is delaying a decision on later years until after their review of local government finance.

This follows a period of sustained growth in local government spending, which increased by 45% during the period 1997 to 2007. The funding reductions come at a time when demographic and recession based factors are increasing demand for some services, and there is a decreasing demand for some services, such as car parking, where customers pay a fee or charge.

Our Approach

Value for Money Conclusion
As part of the work informing our 2010/11 Value for Money (VfM) conclusion we have undertaken 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.

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;
- It's approach to strategic financial planning;
- It's approach to financial governance; and
- It's approach to financial control.

Further detail on each of these areas is provided in the sections of the report that follow. In overall terms the conclusion from this report is that the Council has adequate arrangements in place for achieving financial resilience.

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

Green	**No cause for concern**. 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 the majority of 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 and not in line with good practice.

Our findings are detailed between pages 6 and 39 of this report.
All findings and recommendations have been discussed with senior officers.

Details of the recommendations can be found on pages 8 and 9.

Overview of Arrangements

Area	Summary observations	Summary level risk assessment
Key Indicators of Performance	• The Council has a good track record of financial management, achieving net underspends in each of the last three years. • Benchmarked key indicators of performance indicate that the Council hold an average level of useable reserves compared to their nearest neighbours. The comparison also highlights a strong position in terms of working capital. However, it is clear that working capital will come under increasing pressure as a result of the CSR and will need to be carefully monitored. • Sickness levels have been showing a reducing trend and current performance reflects well against both public sector and private sector averages. Absence management will be a particular challenge for all authorities going forward, given the context of significant pressures on staff to deliver 'more for less' • The current levels of borrowing indicate a reasonably resilient position for the Council and are well within the Councils own prudential limits, although recent trends show a variable degree of short term borrowing to meet the cash flow requirements of emerging expenditure. It is acknowledged that the Council has given consideration to early repayment of long term borrowing, but this is not feasible due to both the size of the applicable penalty payments and also the need to reach agreement with other Councils. • The Council will need to carefully monitor these financial indicators to ensure that it remains financially resilient during the MTFS period.	Green
Strategic Financial Planning	• The Council was able to undertake the most recent MTFS process with an effective lead in time and the process had a high level of stakeholder engagement. • The Council has strengthened its financial planning process in light of the Government's deficit reduction programme. It is clear that the Council took account of its corporate priorities when setting what was a challenging budget. • Key to the MTFS is also how the Council manage their capital going forward. It is intended that a significant proportion of the proposed programme will be funded from available capital receipts. This could prove challenging given the current economic outlook. In addition to this, there may be a requirement for the Council to undertake borrowing in the medium term. The Council must closely monitor the potential risks around the funding of the plan. • The Council will need to continue to monitor the MTFP during its delivery, in particular in relation to the impact of price inflation in the medium term, and the outcome of the Government's funding settlement for financial planning beyond 2012/13. In addition, work is still required to monitor and revisit savings assumptions in the latter years of the strategy to ensure that all potential savings are realised.	Green

Overview of Arrangements

Area	Summary observations	Summary level risk assessment
Financial Governance	• The Council has good senior management and member engagement in financial planning and financial management as part of the Corporate Business Planning process. • The Council has a well established approach and appropriate processes in place in relation to financial governance and has delivered good results in recent financial years. • Following changes to the Constitution with effect from April 2011, the Finance and Performance and Partnership sub-committees of the Overview and Scrutiny Committee have been deleted, with the finance element incorporated into the role and responsibilities of the new Finance, Audit and Risk Committee. It was noted, however, that the 2010/11 Revenue Outturn, 2010/11 Capital Outturn and Risk Management Update reports submitted to the June 2011 meeting were not considered by committee members due to a perceived lateness of papers. The Council will need to ensure that sufficient scrutiny is maintained throughout this period of economic and financial uncertainty. • The finance reports provided for Cabinet provide a detailed narrative regarding the performance of the Council. The reports include a detailed breakdown of variances to budget, including comments against each. • The Council have recognised the importance of a clear understanding of financial information. Review of all reports presented to Committee identifies that financial implications must be considered in all cases.	Green
Financial Control	• The Council has a robust approach to financial and performance management and associated financial controls. • The Council has a good record in controlling spend and in achieving efficiencies and savings. • In year monitoring reports are considered monthly by corporate management team and submitted quarterly to the Overview and Scrutiny sub-committee and Cabinet itself. Specific reporting is included regarding Key Corporate 'Health' Indicators and the Red/Amber/Green (RAG) status of efficiency proposals, with additional detail provided for variances to date against budgets at red or amber status. A review of 2010/11 monitoring suggests that effective monitoring, reporting and escalation has occurred in year. • Overall performance against budget suggests that the Council has a good track record of delivering savings and finding efficiencies, however, the exclusion of specific performance reporting against planned efficiencies as part of year end outturn reporting means that the final position is not directly highlighted to members in the context of the planned savings and that other contributing factors may be responsible. The Council plans to introduce changes to year end reporting to address this issue. • It is anticipated that the Shared Internal Audit Service (SIAS) will increase resilience and give a greater economy of scale to allow access to specialist audit skills. However, to all members of the shared service, it is vital that quality is high and that each member is provided with sufficient levels of IA work and assurance. The Council must ensure that suitable monitoring arrangements are put in place to maintain a high standard of internal audit support.	Green

Recommendations

Area of review	Recommendations	Responsibility	Timescale	Comment
Key Indicators of Performance	The Council should continue to maintain appropriate levels of reserves and monitor the Council's liquidity and other key financial ratios, specifically in relation to usable capital receipts, to ensure financial resilience is maintained. The introduction of additional cash flow forecasting methods should be considered in relation to any potential need for future borrowing.	Head of Finance Accountancy Manager	Ongoing March 2012	Agreed This will be considered in the timescale stated
Strategic Financial Planning	The specific impact of fluctuations in interest rates should be more clearly considered in relation to the adequacy of the Councils annual and medium term budgeting assumptions.	Strategic Director of Finance, Policy & Governance	July 2012	The Medium Term Financial Strategy contains reference at point 16 to the fact that the Council is using the current low interest rates to ensure the budget is less reliant on interest income. At paragraph 9.46, reference is made to a 0.5% change in interest rates equating to a £200k change in income. The impact of a further reduction in interest rates is covered in the financial risks assessment. The 2012 review of the MTFS will consider this point.
Financial Governance	Following reorganisation and restructuring of it's scrutiny committees with effect from April 2011, specific measures should be considered to ensure that the planned level of scrutiny is sufficiently maintained.	Head of Finance	In place	This is included within the terms of reference of the Finance, Audit & Risk Committee for which the Head of Finance is lead officer. Financial reports are taken to this Committee on a regular basis. These include details of how the Council is performing against it's key income targets and the delivery of efficiencies.

Recommendations

Area of review	Recommendations	Responsibility	Timescale	Comment
Financial Control	The Council should ensure that suitable monitoring arrangements are put in place to maintain a high standard of Internal Audit support following the creation of the Shared Internal Audit Service (SIAS).	Head of Finance	December 2011	The Head of Finance is the lead officer for liaison with SIAS. Monitoring, co-ordination and feedback arrangements are being developed in conjunction with the SIAS Audit Manager for NHDC and also with assistance from the Performance & Risk Manager. The Covalent performance system will also be utilised to track progress internally with regards to implementation of agreed audit recommendations.

Section 2

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:

- Out-turn against budget
- Useable Reserves levels
- Working capital ratio (liquidity)
- Borrowing levels
- Sickness absence levels

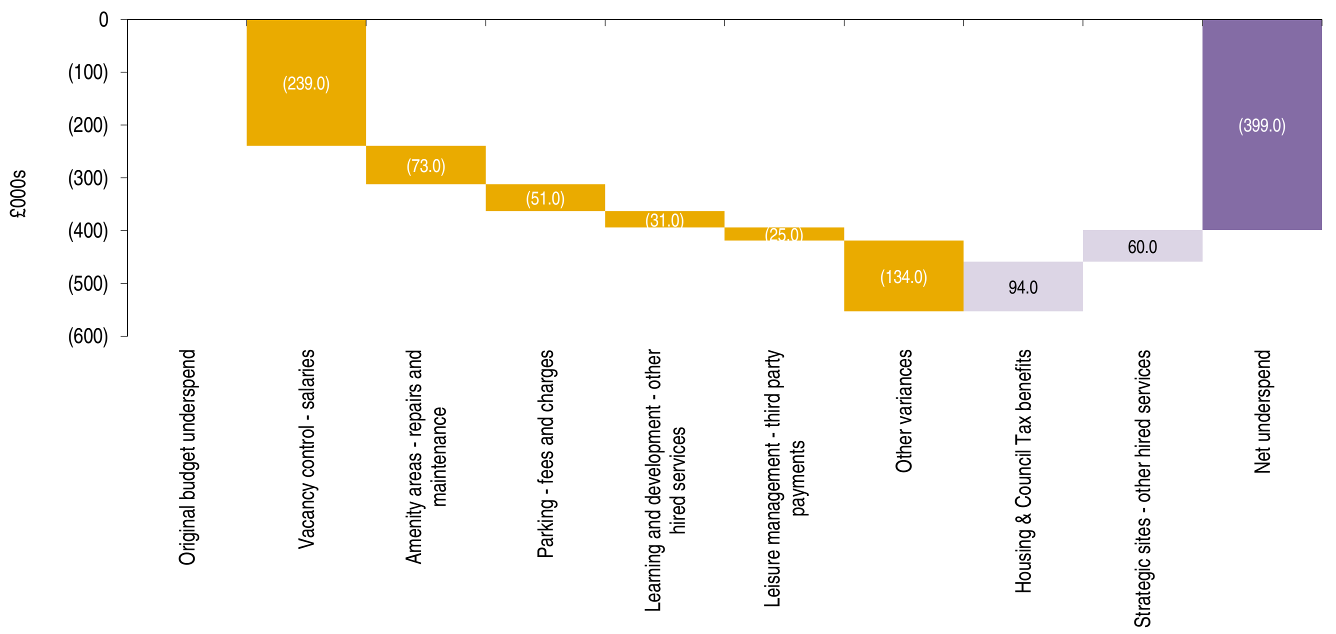
We have used the Audit Commission's 'nearest neighbours' benchmarking group, which is the following authorities.

- Ashford Borough Council
- Braintree District Council
- Colchester Borough Council
- Dacorum Borough Council
- Epping Forest District Council
- Hertsmere Borough Council
- Maidstone Borough Council
- *North Hertfordshire District Council*
- Rugby Borough Council
- Stroud District Council
- Taunton Deane Borough Council
- Test Valley Borough Council
- Tonbridge & Mailing Borough Council
- Tunbridge Wells Borough Council
- Vale of White Horse District Council
- Welwyn Hatfield Borough Council

Overview of performance

Area of Focus	Summary observations	High level risk assessment
Performance Against Budget	• Quarterly reporting to Cabinet supports that an effective monitoring framework is in place at the Council, which is reflected in part by in year 'working' budget revisions to take effect of identified significant variances from plan. • The Council has a good track record in managing expenditure against budget, achieving net underspends against its working budget in each of the last three years. This is highlighted in the graph below:  • The setting and approval of the original annual revenue budget is noted to be underpinned by efficiency and investments options proposals, approved following discussions at Member workshops and Area Committees. In its draft financial statements the Council states that ongoing efficiencies of over £1.3 million were achieved in 2010/11.	Green

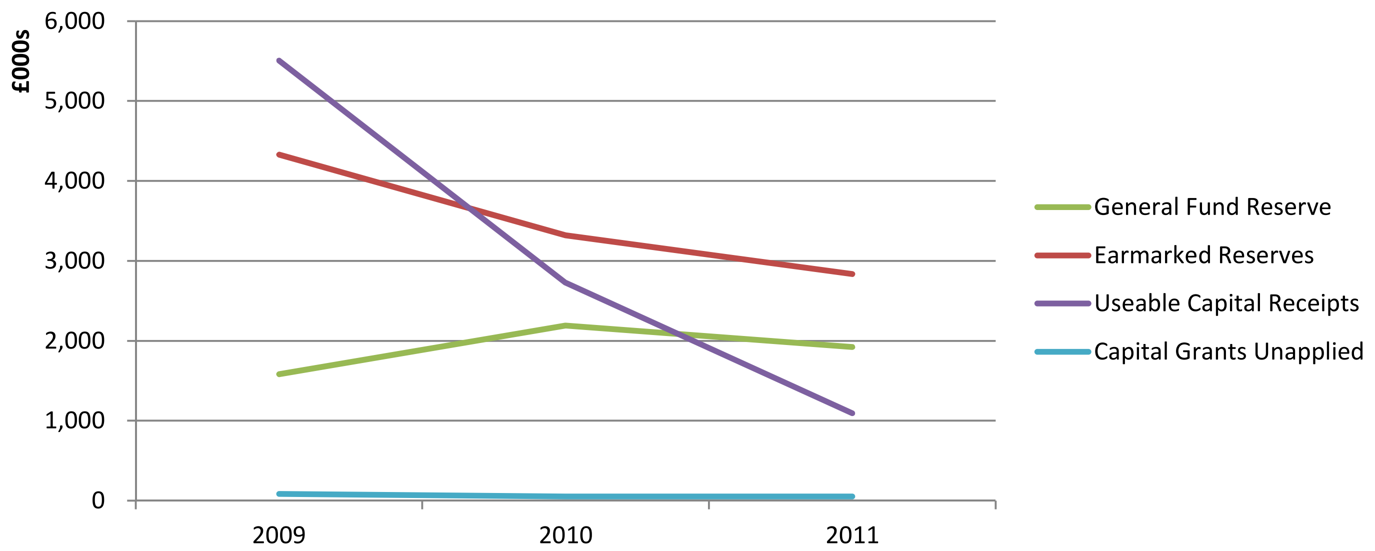
Overview of performance

Area of Focus	Summary observations	High level risk assessment
Performance Against Budget (continued)	• The 2010/11 outturn is based on the amounts per the draft financial statements. A waterfall graph highlighting the major variances from the working budget is shown below:  • The most significant variance was observed in relation to planned vacancy control activity, with the majority of the variance reported to be due to the incidence of more manageable vacancies than were originally identified, lower than anticipated redundancy costs as a result of a number of redeployments, and the number of vacancies held across various services.	

Overview of performance

<table>
<tr><th>Area of Focus</th><th>Summary observations</th><th>High level risk assessment</th></tr>
<tr><td>Reserve Balances</td><td>

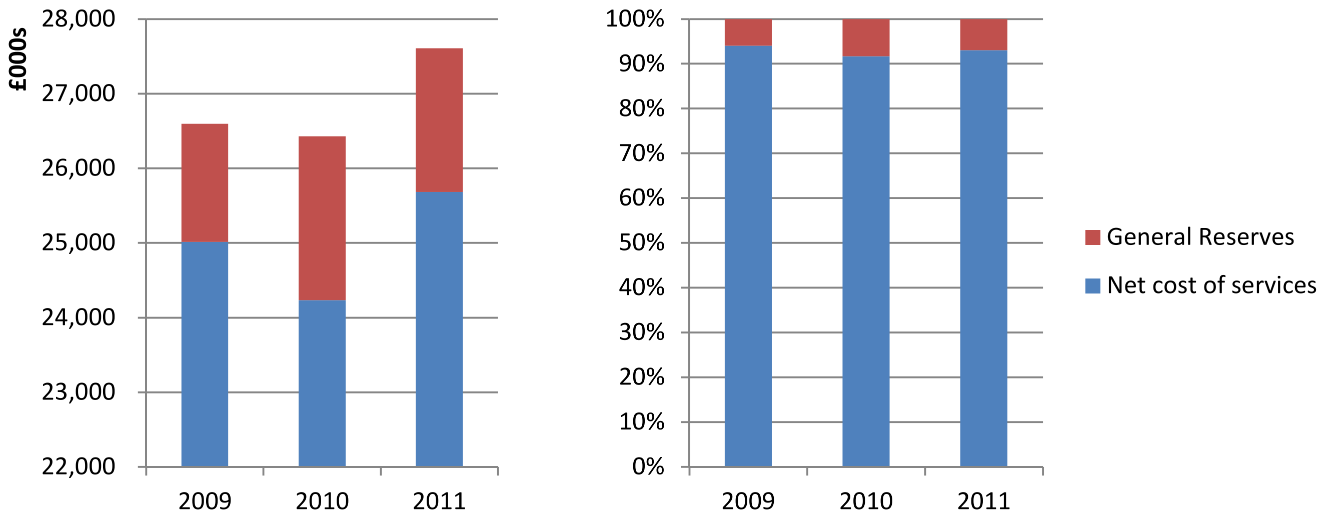
- The Council's usable reserves have reduced from £11,505k to £5,904k over the three most recent years. However, as the graph below shows, the key driver from this reduction is the level of the capital receipts reserve:



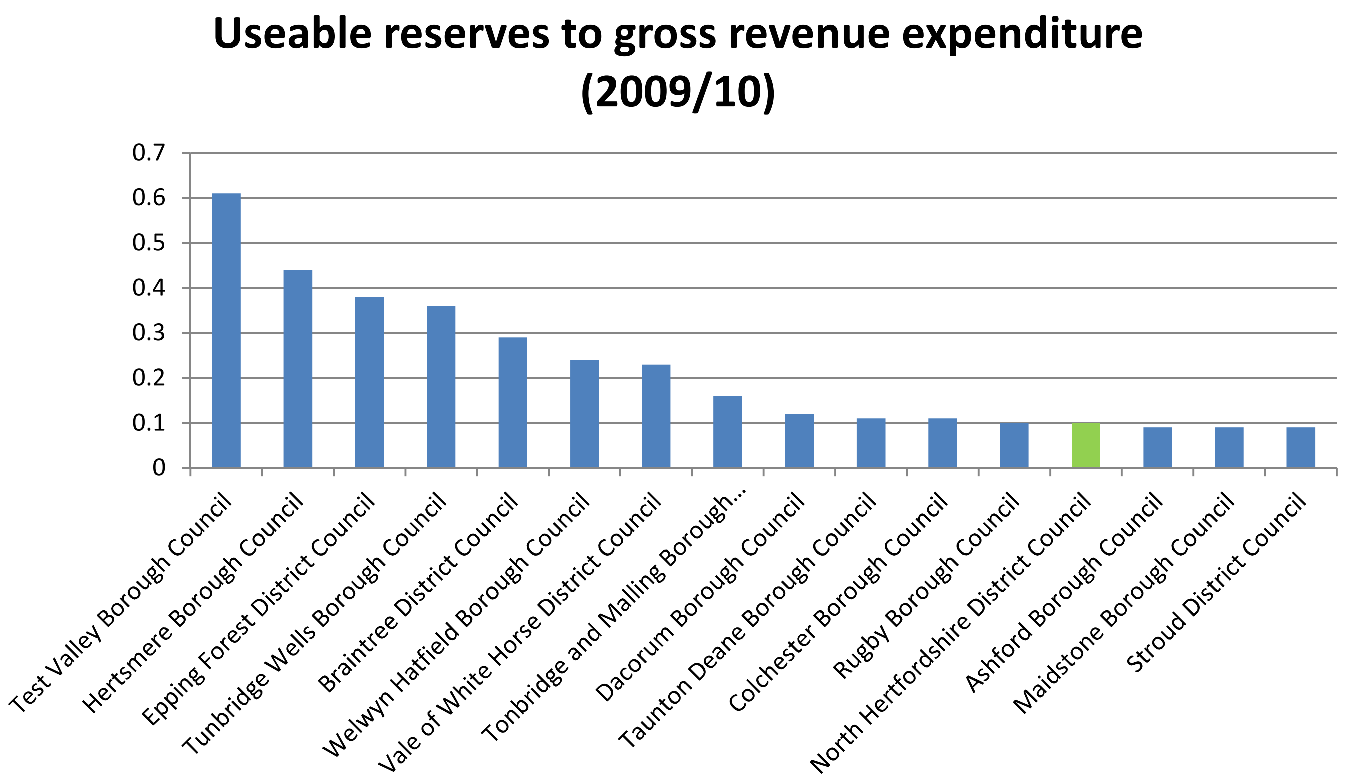
- The balance of the capital receipts reserve has fallen from £5,507k in 2009/10 to £1,093k in 2010/11, a drop of 80%. In the current economic climate it is difficult to sell assets to provide additional funding, hence the rapidly reducing level of the reserve. A review of the capital programme was completed by the Council in early summer of 2010/11 and the original capital programme for the year of £11,279k reduced to a working budget of £7,142k. Receipts of £4,731k continue to be anticipated rom asset sales in 2011/12, increasing the potential requirement of borrowing.

</td><td>Amber</td></tr>
</table>

Overview of performance

Area of Focus	Summary observations	High level risk assessment
Reserve Balances (continued)	• The graphs below show the level of general reserves against the net cost of services balance. The first graph shows this in actual terms, the second in percentage terms. *(NB. the impact of the £14,988k negative credit resulting from the central government decision to change the pension increase rate from RPI to CPI has been excluded from the 2010/11 net cost of services for comparison purposes)*  • This highlights that whilst the level of reserves has fallen over the previous three years, as a percentage of the net cost of services the level has remained relatively consistent and at a level that achieves the Council's target minimum balance of 5% of net expenditure. This evidences that the Council is maintaining reserves at a reasonable level.	

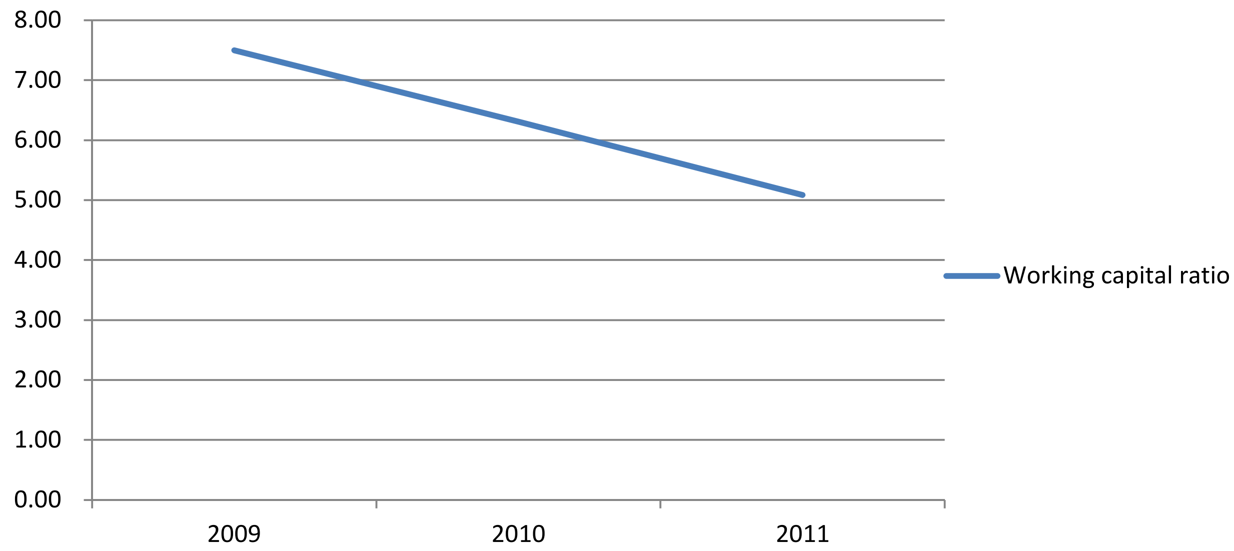
Overview of performance

Area of Focus	Summary observations	High level risk assessment
Reserve Balances (continued)	• The Audit Commission made comparative data available for 2009/10. This has been used to generate the graph below showing the ratio of usable reserves to gross revenue expenditure with a comparison against those authorities the Audit Commission considers to be 'nearest neighbours'.  • This shows the Council holds an average level of reserves compared to their 'nearest neighbours'.	

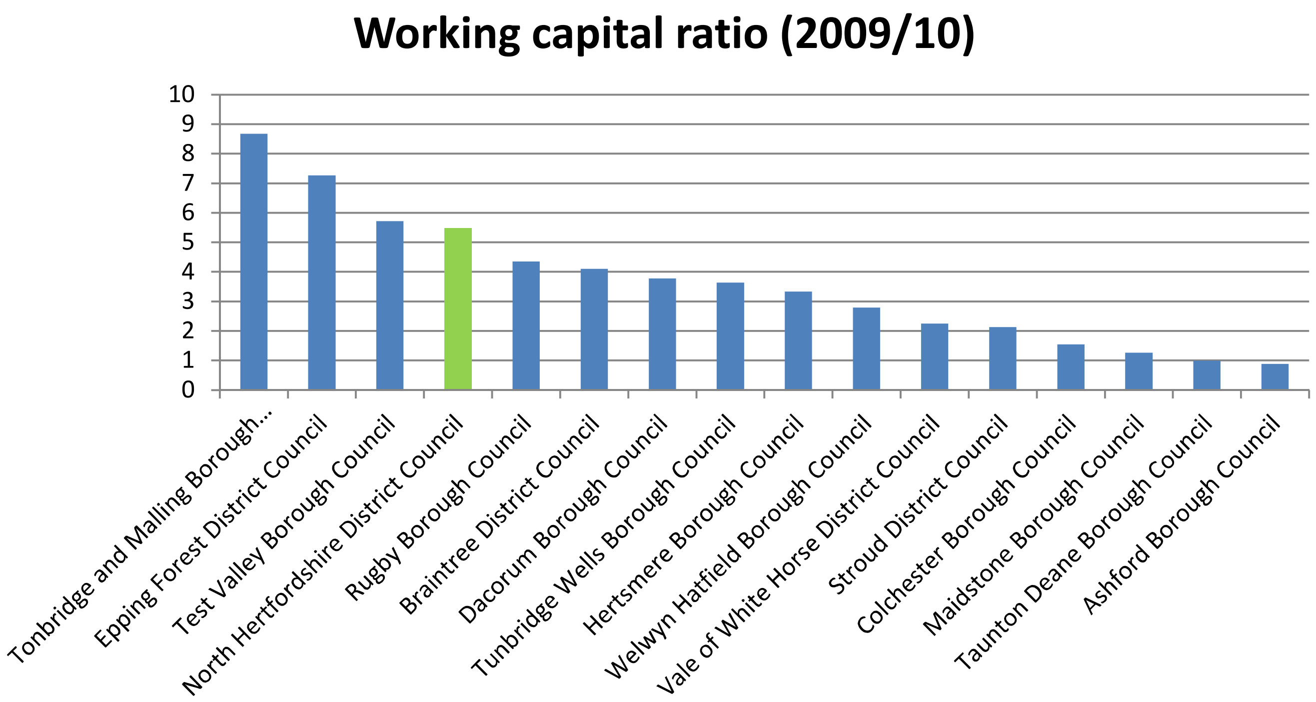
Overview of performance

Area of Focus	Summary observations	High level risk assessment
Reserve Balances (continued)	• It remains important, and is perhaps even more critical, to maintain appropriate levels of General Fund reserves during this period of fiscal constraint. Failure to do so may create cash flow pressures and, in turn, cause adverse publicity for the Council. • The Council continues to maintain a specific 'special reserve' to meet the short term needs of maintaining appropriate levels of General Fund reserves. Because the net spend in 20101/11 was lower than anticipated it was not necessary to transfer any funds from the special reserve into the general fund balance in order to maintain the minimum General Fund Balance of £1,638k approved by members. The projected general fund and special reserve balances have therefore been revised and reapproved to accommodate the actual outturn position. • The Medium Term Financial Strategy (MTFS) recognises the importance of maintaining sufficient balances to deal with unforeseen events and to cover the potential risk of not achieving required savings levels.	

Overview of performance

Area of Focus	Summary observations	High level risk assessment
Liquidity	• The working capital ratio indicates if an authority has enough current assets, or resources, to cover its immediate liabilities - i.e. those over the next twelve month period. As the graph below shows, the Council's working capital ratio has fallen over the three years 2008/09 to 2010/11.  • This indicates that the Council's liquidity is decreasing, although it should be noted that it remains at a high level. A ratio of assets to liabilities of 2:1 is usually considered to be acceptable, whilst the Council currently have a ratio of just over 5:1. In general, a very high working capital ratio is not considered to be a good thing, as it tends to indicate that an entity is not investing its excess cash effectively. However, North Herts have invested the cash but, due to the nature of the investments, this remains reported as a current asset. Were these investments to be excluded from the calculation the revised current working capital ratio would be 1.51:1 which is indicative of an underlying position that would not be considered unreasonable.	Green

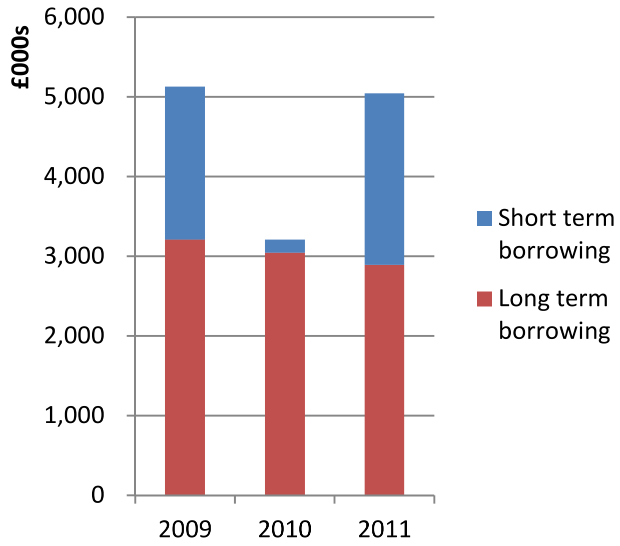
Overview of performance

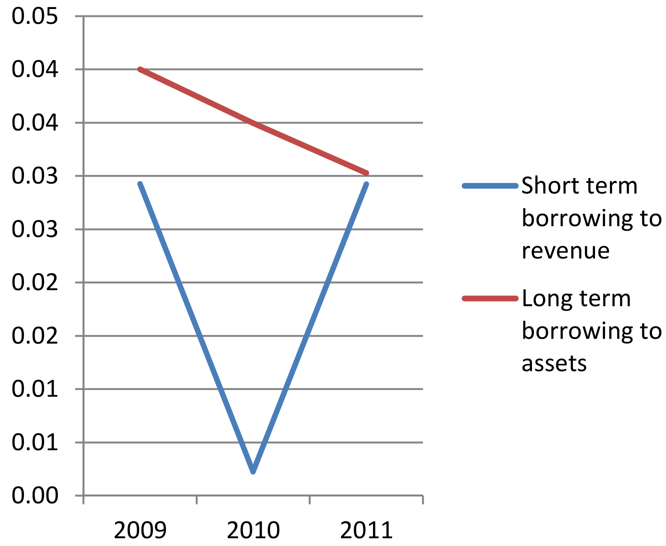
Area of Focus	Summary observations	High level risk assessment
Liquidity (continued)	• As with usable reserves, the Audit Commission made comparative data available for 2009/10. This has been used to generate the graph below showing the working capital ratio with a comparison against those authorities the Audit Commission considers to be 'nearest neighbours'.  • In the context of its 'nearest neighbours' the Council is maintaining a positive working capital ratio and looks to be in a strong position, as evidenced by the comparison above. However, it is clear that working capital will come under increasing pressure as a result of the Spending Review and will need to be carefully monitored.	

Overview of performance

<table>
<tr><th>Area of Focus</th><th>Summary observations</th><th>High level risk assessment</th></tr>
<tr><td>Borrowing</td><td>

- The first graph shows borrowing balances for both long and short term borrowing in actual terms at balance sheet dates, the second graph shows the respective ratios between long term borrowing and assets and short term borrowing and revenue:

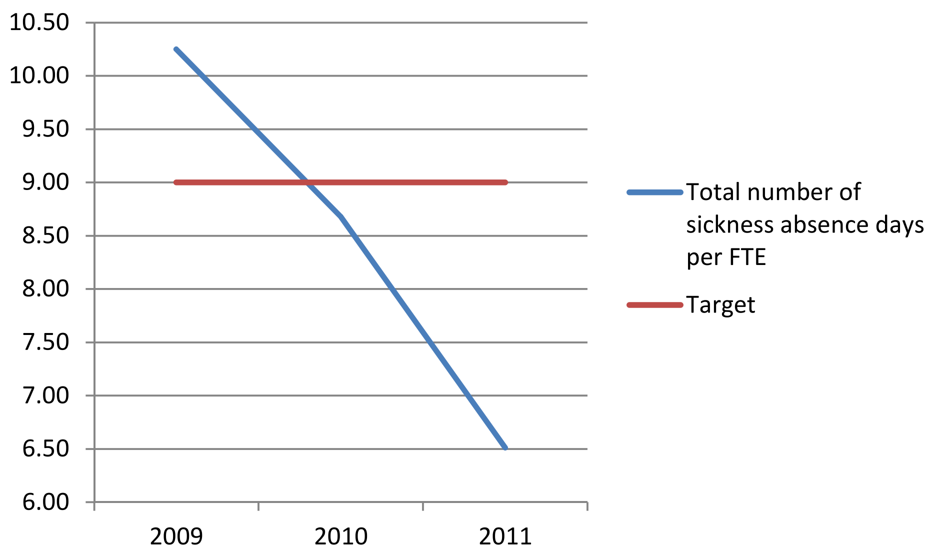




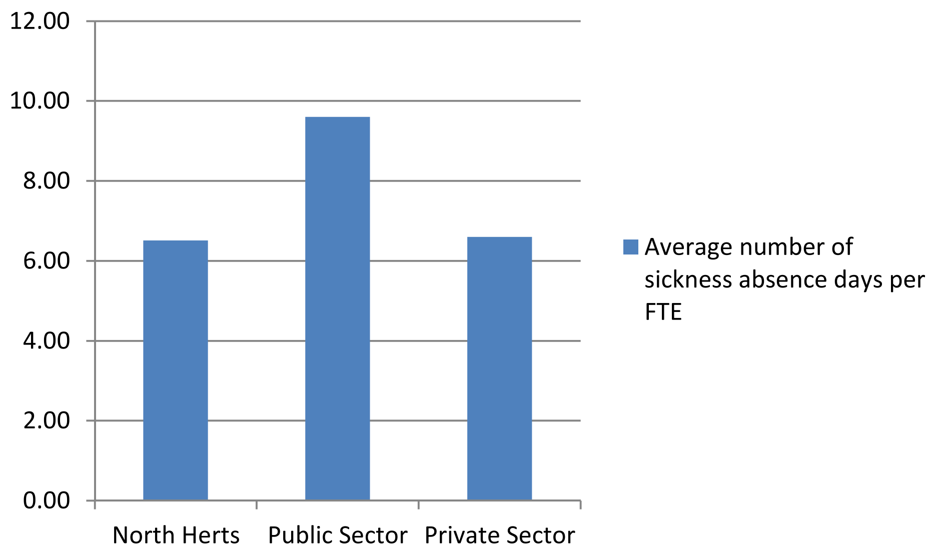
- The current levels of borrowing indicate a reasonably resilient position for the Council and are well within the Councils own prudential limits, although recent trends show a variable degree of planned and approved short term borrowing to meet cash flow requirements of emerging expenditure. It is acknowledged that the Council has given consideration to early repayment of long term borrowing, but this is not feasible due to the size of the applicable penalty payments relative to the value of balances currently held.
- Prudential borrowing is an area that the Council has acknowledged to it's members it will need to monitor going forward, particularly to fund the on-going capital programme. The level of the capital receipts reserve is reducing and with difficulty of obtaining significant capital receipts, there may need to be additional borrowing going forward.

</td><td>Amber</td></tr>
</table>

Overview of performance

Area of Focus	Summary observations	High level risk assessment
Workforce	• The Council's sickness absence levels have been showing a reducing trend over the past three years, with the estimated figure for 2010/11 down to just over 6.5 days. As the graph below shows, the Council have also moved to consistently performing ahead of target.  • The Council reviews absence levels as part of it's regular performance monitoring activity, and it will be important that workforce issues continue to be carefully managed when they arise and that a robust approach to sickness absence monitoring is maintained in order to sustain the improving trend.	Green

Overview of performance

Area of Focus	Summary observations	High level risk assessment
Workforce (continued)	• The graph below shows that performance at the Council reflects well against both public sector and private sector averages:  • Costs that accrue from sickness absence relate to the hiring of agency staff to cover staff gaps, or from holding a larger workforce complement than is desirable. Absence also damages service levels either through staff shortage or lack of continuity. Reducing absenteeism saves money, improves productivity and can have a positive customer benefit. Absence management is expected to be a particular challenge for all authorities going forward, given the context of significant pressures on staff to deliver 'more for less'.	

Section 3

Strategic Financial Planning

Key indicators of good Strategic Financial Planning	• Focus on achievement of corporate priorities is evident through the financial planning process. The MTFS focuses resources on priorities. • Service and financial planning processes are integrated. • The MTFS 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 MTFS 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 SR10. • The MTFS 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 MTFS. • Effective treasury management arrangements are in place. • The council operates within an appropriate level of reserves and balances.

Medium Term Financial Strategy

Area of Focus	Summary observations	High level risk assessment

Focus of the MTFP	• The MTFS is set up so to establish the Council's strategy for the next five years and to set out the financial challenges that the Council will face over this medium term.
	• The Council have recognised that planning now to meet known changes in the future helps to provide greater opportunity to phase in the impact of the changes. An updated Medium Term Financial Strategy (MTFS) has been prepared that covers the period 2011/16 and an approved MTFS has already been developed for the period 2012/17. The strategy emphasises the need to address uncertainty in the planning process resulting from both the outstanding final announcement of local government finance settlement figures and the current consultation on the future use of Business Rates.
	• Prior to the announcement of the 2011/12 settlement by CLG, the Council developed plans based on expected reductions in the formula grant and a freeze on Council Tax. By anticipating the potential reductions at an early stage the Council was able to prepare proposals for significant cost reductions.
	• A number of changes have been implemented in the last two years to further improve the Council's financial management strategy, namely to:
	  • Identify how much the Council spends against each strategic priority
	  • Identify the areas that are lower or non priority for allocation of resources including review of statutory and discretionary services
	  • Review the level of income generated by services that charge compared to the costs of provision
	  • Reduce future reliance on interest rate income
	  • Amending the Council Tax "rule" to reflect the impact of the current negative RPI figures.
	• Review of the MTFS makes it clear that the strategy is applying resources so as to achieve the Council's priorities.
	• Key to the MTFS is also how the Council manage their capital going forward. As with the MTFS, the capital programme is focussed on the achievement of the Council's priorities. All proposed schemes are scrutinised in detail by the Corporate Management Team to ensure that projects are in line with these priorities and that all projects are phased appropriately and in line with available resources.
	• It is intended that a significant proportion of the proposed programme will be funded from available capital receipts. This could prove challenging given the current economic outlook. In addition to this, there may be the requirement for the Council to undertake borrowing in the medium term. The report on the capital programme taken to Cabinet acknowledges the potential risks around the funding of the plan and highlights the need for both prudence and on-going monitoring.
		Green

Medium Term Financial Strategy

Area of Focus	Summary observations	High level risk assessment

Adequacy of planning assumptions	• The first two years of the strategy assume 0% pay increase for those earning more than £21k pa and 2% thereafter, whilst known pay increments due in 2011/12 and estimated future increases in superannuation contributions that may be required to meet the liability in the pension fund have been built into the model.
	• No allowance is made for general price inflation on expenditure outside of contracted activity. The Government's ongoing inflation target is 2%. CPI inflation was 4% in March 2011 and the Bank of England's most recent forecasts suggest inflation will remain above the 2% target level throughout 2011/12. Whilst inflation is forecast to fall during 2012 and 2013, the timing and extent of any fall remains highly uncertain and may therefore have unforeseen impacts on costs and 'consumer' behaviour during the period covered by the current MTFS.
	• The current MTFS notes that there are a number of key risks in the assumptions after 2012/13 due to uncertainty around the potential final outcome of the Local Government resource review. The key issues are identified as follows:
	  • Implications of the Welfare Reform Bill and the introduction of the Universal Credit
	  • The Government's announced intention to localise business rates
	  • The final announcement of the outcome of the Local Government resource review, which is expected in late 2011
	• The impact of minor percentage variations in interest rates and Council Tax brought to Members attention in assessing the basic assumptions included in financial plans.
	• The final section of the current MTFS presents alternative scenarios regarding the future uncertainty in relation to the amount of government funding , included anticipated changes such as additional New Homes Bonus income, and the impact that this could have on planned efficiency targets. The scenarios currently modelled range from amounts being frozen at the 2012/13 settlement, up to a 20% further reduction spread evenly over the subsequent four years. The expected position presented is a further 8.9% reduction after 2012/13 (1.9% in 2013/14 and 7% in 2014/15).
	• Benchmarking is used to determine the adequacy of assumptions on fees and charges where there is local discretion (such as car parking, cremations and allotments) and for rates to be competitive with neighbouring Councils.
	• Part of dealing with the cost pressures faced by the Council is the achievement of savings targets. These savings are seen as being of vital importance in order for the Council to maintain a strong level of general balances. In terms of the savings required, the Council is felt to be in a strong position, with the statement made within 2011/12 quarter 1 reporting that of the £1.913m of expenditure reduction and income generation proposals agreed in the 2011/12 original budget £1.737m (91%) is expected to be achieved.
		Amber

Medium Term Financial Strategy

Area of Focus	Summary observations	High level risk assessment
Scope of the MTFS and links to annual planning	• The Council's current published MTFS effectively covers the period 2011/16. and recognises that public services are being faced with meeting unprecedented challenges in how Councils are run and the services that they are able to deliver. • The MTFS is the Council's stated key financial planning document as part of a priority led budgeting process and is designed to complement the Council's Corporate Plan. The Corporate Plan sets out the Councils priorities and the MTFS sets out how the financial management process is expected to deliver against them. Both documents are an integral part of the Corporate Business Planning process. • The Corporate Business Planning timetable is well established and sets out the various stages to arriving at the final annual budget alongside consideration of the MTFS and the Council's ongoing priorities. Whilst this provides an established framework, timings are flexed from one year to another in order to accommodate additional economic factors and government announcements. The finance team produce reports in support of the various key stages, which ensures a culture of consistently meeting relevant reporting deadlines and reinforcing the link to the Council's priorities.. • The Council always aims to set a balanced budget. Based on the changes to the settlement position, the proposed efficiencies targets were revisited and additional expenditure reduction and income generation proposals used to bridge the gap. This meant that there were reductions in certain areas of spend, including some priorities, but ultimately that no priorities were changed. • Changes to the timetable demonstrated in response to the recent economic downturn and SR10 include more revisiting of assumptions to Challenge Board and an earlier consideration of service expenditure, which included the overall spread of spend and whether services were statutory or discretionary in considering the potential for reductions. Heads of Service were directly asked how reductions of up to 25% could be achieved in current budgets. • The current MTFS presented to and approved by Cabinet in July 2010 covers savings and growth targets for the 2011/12 budget process. As the strategy notes, the Council made significant progress against saving requirements by developing a strong savings package for 2011/12. • Savings proposals are identified by officers and are then taken to Scrutiny, a meeting that all members are able to attend. The Council provide their members with a long list of potential savings and set out the required savings target. The members are then responsible for selecting those savings that they feel are the most appropriate. Clearly, this means that things can be saved, but at the expense of others. • The budget for 2011/12 was approved by Cabinet in January 2011. The report supporting this clearly links back to the MTFS set in July 2010 and the savings proposals agreed at the October and November 2010 workshops. • There is evidence that both senior officers and members debated and challenged budgets and savings across all services.	Green

Medium Term Financial Strategy

Area	Summary observations	High level risk assessment
Review processes	• The Council have a clear process in place for the preparation of the MTFS through to the final budget. • In July 2010 the detailed MTFS covering the period 2011/16 was taken to Cabinet for approval. This followed detailed review of the assumptions contained within the strategy and the savings proposals by the Challenge Board and Scrutiny committees. The MTFS supports the planning process and helps to identify the resource issues and principles that will shape annual budget development. • The review process highlighted the Council's response to the economic downturn. They recognised potential impacts on the MTFS and senior officers then identified and took potential savings to Challenge Board, Area Committees, Scrutiny meetings and Members workshops to enable Members to have a clearer understanding of potential options and their respective impact. • In preparing the MTFS, senior officers take account of all available information sources to produce a financial forecast for the medium term. As part of this process, the efficiency target to maintain the agreed minimum general fund balance is identified. A timetable is then put in place for identifying these savings. This process involves Members, key finance staff, Portfolio Holders, Heads of Service and senior management. In addition to this, the Council have an established number of key stakeholders with whom consultation regularly takes place. • Following the MTFS in July 2010, the strategy was re-considered and updated where necessary as part of a corporate business planning document (Strategic Approach to Budget Setting in 2011/12 to 2015/16) presented to Cabinet in September 2010, in preparation of autumn workshops, and in the 2011/12 provisional and working budget setting reports that went to Cabinet in December and January respectively. • Clearly, with significant efficiency targets in place, there are inherent risks within the strategy. Officers are clearly aware of this, and there are significant monitoring arrangements in place, including regular corporate healthcheck reports going to both Scrutiny and Cabinet.	Green

Medium Term Financial Strategy

Area	Summary observations	High level risk assessment
Responsiveness of the Strategy	• It is clear from review of minutes and reports around the finances of the Council that the MTFS is being monitored closely and any changes being taken into account. If there are any material changes required, for example emerging proposals or government announcements around the next finance settlement, then the strategy would be revised and presented to Members. • The MTFS is updated each year as part of the annual Corporate Business Planning cycle. All changes are monitored on an on-going basis. • The current MTFS presented to Cabinet in July 2010 was updated to reflect all government announcements on public finances, as well as trying to anticipate potential announcements that may be still to come, as delaying production of the 2011/16 MTFS until after the results of the Local Government Resource review was discounted by the Council due to the perceived need to commence work early to identify the challenging efficiency options that would be required to close the expected funding gap. Until the outcome of the review is known, detailed financial planning beyond 2012/13 remains based on assumptions. The Council intends to revisit the MTFS in the next few months, once there is greater clarity at the national level. • It is clear that budgetary pressures could arise due to a number of risk based factors and that a relatively small change to inflation levels (where not already considered as part of contracted activity), pay awards, government funding or demand could result in significant impacts on need to identify and achieve further savings. • Ultimately, it is felt that all savings included within the plan should be achievable. However, the achievement of savings is considered as part of the risk assessment of reserve balances. • In year monitoring reports are considered monthly by corporate management team and submitted quarterly to the Overview and Scrutiny sub-committee and Cabinet itself. Specific reporting is included regarding Key Corporate 'Health' Indicators and the Red/Amber/Green (RAG) status of efficiency proposals, with additional detail provided for variances to date against budgets at red or amber status. A review of 2010/11 monitoring suggests that effective monitoring, reporting and escalation has occurred in year.	Amber

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Section 4

Financial Governance

Key indicators of effective Financial Governance	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 • The CFO is a key member of the leadership team • Officers and managers across the council understand the financial implications of current and alternative policies, programmes and activities • The leadership ensure appropriate financial skills are in place across all levels of the organisation • The leadership foster an open environment of open challenge to financial assumptions and performance. There is engagement with stakeholders including budget consultations. There are comprehensive policies and procedures in place for Members, Officers and budget holders which clearly outline responsibilities. A small 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).

Understanding and engagement

Area of focus	Summary observations	High level risk assessment
Understanding the Financial Environment	• The Council's Corporate Business Planning process facilitates a critical review of existing expenditure through the work of the Challenge Board of officers led by the Chief Executive. This group reviews the base position, challenges existing budget allocations and creates the ability to reallocate money to strategic priorities. • The 2010/11 annual revenue budget was approved at the Cabinet meeting in January 2010 accompanied by presentations from both the Leader of the Council and the Portfolio Holder for Finance. Draft plans had been presented to Cabinet in December 2009 accompanied by efficiency and investment proposals following discussion at Member workshops and Area Committees in November and December 2009. The same process has been followed for 2011/12, with additional consideration given regarding the timing of Local Government Settlement announcements. Existing functions of the Council are now being included in ranking against the Council's scoring matrix and it is anticipated that this ranking will be used in the autumn workshops again to assist in deprioritisation of functions. • Minuted discussions at Cabinet support that specific consideration is given to the political acceptability of savings and service reductions as well as their wider impacts to overall service delivery, with the following recommendation having been recorded from the Scrutiny Committee: "That in respect of the Revenue Budget 2010/11, the proposal not to inflate grants to organisations should be subject to further consultation, inviting the organisations concerned to notify the Council of any adverse impact on their agreed service". • The role of Members and officers of the Council in the Corporate Business Planning process is clearly defined in section 3 of the MTFS. • Financial planning and financial management is challenged and scrutinised at member level through both Cabinet and Finance Scrutiny, receive both regular reports on the financial planning and monitoring processes and is proactive in requesting special reports on matters of interest and concern. When necessary these are escalated for comment and action. Following changes to the Constitution with effect from April 2011, the Finance and Performance and Partnership sub-committees of the Overview and Scrutiny Committee have been deleted, with the finance element incorporated into the role and responsibilities of the new Finance, Audit and Risk Committee. It was noted, however, that the 2010/11 Revenue Outturn, 2010/11 Capital Outturn and Risk Management Update reports submitted to the June 2011 meeting were not considered by committee members due to a perceived lateness of papers. The Council will need to ensure that sufficient scrutiny is maintained throughout this period of economic and financial uncertainty. • Senior management performs challenge and scrutiny through the Challenge Board. This is noted to have been significantly strengthened by the adoption of the corporate business and VfM strategies, whereby service reviews require the demonstration of efficiencies in cost and improvement in service performance. • The finance reports produced for Cabinet provide a detailed narrative regarding the performance of the Council and a detailed breakdown of variances to budget including comments against each.	Green

Understanding and engagement

Area of focus	Summary observations	High level risk assessment
Executive and Member Engagement	• Review of the budget setting process indicates that there is considerable engagement in the process both from senior officers and from members. • As noted previously, there is a significant degree of consultation around the proposed efficiencies plans. This included Members Workshops and Area Committees and involved both Scrutiny and the Cabinet, enabling all Members to comment on the plans and process. • Financial monitoring and reporting is an integral part of the Council's Corporate Business Planning process. Both managers and members receive regular reports that suit individual needs, as reviewed and considered by the respective recipients, but with the common purpose of being timely, up to date and sufficiently forward looking. The reports ensure that variances are identified in a timely manner, that the impact on both budget and performance is understood and where necessary appropriate remedial action is taken to improve on performance or budgetary control. Emphasis is placed upon the impact of variances on both the Council's priorities and its reserves and future financial position. • The regular reporting of Key Corporate Financial 'Health' Indicators, which are linked to outputs and wider performance indicators is of particular relevance in the current economic climate in assisting the Council to identify, understand and respond to financial pressures and their impact on service delivery. • Training is focussed on new members, and consideration given to the financial reporting experience of members, to ensure that they are familiar with financial areas that require consideration and scrutiny as part of the Corporate Business Planning process. In addition to this, monitoring reports include details of any legal implications and financial and risk implications in order to aid understanding of potential impacts. Details of contact officers and relevant background papers are also included should members require further consultation or explanation of the content of committee reports.	Green

Monitoring and review

Area	Summary observations	High level risk assessment

Review of accuracy of Committee reporting	• The Council provides an online up to date financial ledger on a commitment accounting basis. Comprehensive monthly budget reports are provided for service managers within 10 working days of each month end for both revenue and capital accounts under their control. Online financial data is robust enough to allow service managers to monitor key aspects of their service. This is reinforced by monthly reports that give a more comprehensive picture e.g. consideration of month end cash income.
	• Review of example Committee monitoring reports have found them to include detailed financial information alongside explanations for variances. Each report is consistently split into the following standard sections:
	  • Background,
	  • General Fund - Income and Expenditure
	  • Trading Accounts - Income and Expenditure
	  • Carry Forward Budgets
	  • Efficiencies and Investments
	  • Key Corporate 'Health' Indicators
	  • Projected General Fund Balances
	  • Use of Earmarked Reserves
		Green

Performance Management of Budgets	• Quarterly committee finance reports include significant detail of variances (+/- £25k or +- 25%) against actual and planned performance. The narrative included within the report provides details of the causes of the variance along with planned corrective action. • The expected overall impact to planned year end general fund balances is shown to be clearly highlighted in quarterly finance reporting in relation to the individual variances identified and has been shown to have been actively discussed in year. • Members approved the General Fund 2010/11 estimates in February 2010 and approved General Fund net expenditure of £18.112m. Changes to the working budget, including both increases and decreases in year, were approved by members following the budget returns for each quarter as well monthly monitoring in at least one instance. The final working budget reported against at year end was £18,515m, with an Actual-Working Budget underspend of £399k. • The Finance Scrutiny Sub Group (now part of the Finance, Audit and Risk Committee) undertakes a consistent degree of discussion regarding the reported financial performance, seeking clarification and additional explanation from senior officers where this is considered to be needed, and frequently ask for additional investigation to be carried out and reported subsequently to the group in any areas of particular interest or concern. • The statement of accounts includes detail on performance against budget and provides explanations for all significant movements.	Green

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Section 5

Financial Control

Key indicators of Effective Financial Control	Budget setting and budget monitoring • Budgets are robust and prepared in a timely fashion and the council has a good track record of operating within its budget • 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, including trend analysis, benchmarking of unit costs, risk and sensitivity analysis. • There is particular focus on monitoring income related budgets The capacity and capability of the Finance Department and Service Departments are fit for purpose Financial Systems • Key financial systems have received satisfactory reports from internal and external audit • Financial systems are adequate for future needs, for example commitment accounting functionality is available Internal Control • Strength of internal control arrangements - 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 is how business risks are managed and controlled. • The Annual Governance Statement gives a true reflection of the organisation.

Internal arrangements

Area of focus	Summary observations	High level risk assessment
Performance against Savings Plans	• Final efficiency plans for 2010/11 were agreed as part of the annual revenue budget at the Cabinet meeting in January 2010 to be recommended to Members for approval February 2010. Draft plans had been presented to Cabinet in December 2009 following discussion at Member workshops and Area Committees in November and December 2009. The same process has been followed for 2011/12 efficiency proposals, with additional consideration given regarding the timing of Local Government Settlement announcements. • Minuted discussions at Cabinet support that specific consideration is given to the political acceptability of savings as well as their wider impacts to overall service delivery, with the following recommendation having been recorded from the Scrutiny Committee: "That in respect of the Revenue Budget 2010/11, the proposal not to inflate grants to organisations should be subject to further consultation, inviting the organisations concerned to notify the Council of any adverse impact on their agreed service". • Efficiency proposals identify the link to priorities expressed in the MTFS, the level of expected recurrent savings, whether they relate to a statutory function and assign a risk rating to their achievement. • In year monitoring reports are considered monthly by corporate management team and submitted quarterly to the Overview and Scrutiny sub-committee and Cabinet itself. Specific reporting is included regarding Key Corporate 'Health' Indicators and the Red/Amber/Green (RAG) status of efficiency proposals, with additional detail provided for variances to date against budgets at red or amber status. A review of 2010/11 monitoring suggests that effective monitoring, reporting and escalation has occurred in year. • Overall performance against budget suggests that the Council has a good track record of delivering savings and finding efficiencies, however, the exclusion of specific performance reporting against planned efficiencies as part of year end outturn reporting means that the final position is not directly highlighted to members and that other contributing factors may be responsible. • In year monitoring of the achievement of 2011/12 planned efficiencies during the first quarter highlights negative variances to date regarding planned savings associated with vacancy control and redundancies due to unforeseen delays and additional costs. Monitoring and reporting in year would be expected to include consideration and identification of other mechanisms to meet and respond to delays or rising costs, or otherwise identify additional sources of compensating income.	Amber
Summary of key financial accounting systems	• The most recent Internal Audit report on the main accounting and budgetary control system (Integra) was produced as a final report dated 11 April 2011. This report assigned 'Substantial to Full Assurance' to the systems and procedures which underpin the Main Accounting System process. This does not highlight any significant areas of concern. • Our information systems specialist performed a high level review of the general IT control environment, as part of the overall review of the internal controls system. We have also performed a follow up of the issues that have been raised in the previous year. We concluded that, from the work undertaken to date, there are no material weaknesses which are likely to adversely impact on the Council's financial statements.	Green

Internal and external assurances

Area of focus	Summary observations	High level risk assessment
Finance Department resourcing and qualifications / experience	• The current staffing level is 8 FTEs across Main Accountancy. This includes the Head of Financial Support Services who holds responsibility for Accountancy at the Council. All members of the team are either CPFA or AAT qualified, with the exception of two staff members who are currently certificate level CIPFA trainees. • The Finance Team at the Council has been in place for a number of years and is made up of staff experienced within their roles. There are no imminent restructuring plans within the department, although there is future potential for a move to shared services with other authorities such as Stevenage Borough Council and East Herts District Council in areas such as the payment of invoices and the sundry debtor functions. • Discussions with senior officers have highlighted the importance of training. Clearly, all qualified accountants are required to complete CPD training on an on-going basis. There are on-going training requirements in place through management development arrangements and staff regularly attend CIPFA courses, with one staff member also now currently studying CIPS. In addition, consultation with appropriate external providers is considered where need for specialist input is identified.	Green
Internal audit arrangements including compliance with CIPFA Code of Practice for Internal Audit	• For the year 2010/11, Internal Audit remained an in-house function at the Council. Performance of the function has been strong over the past few years and the overall level of plan completion was good. • The overall Internal Audit opinion for the 2010/11 financial year concluded that an effective internal control environment was in place with regard to key financial systems and that an adequate internal control environment was in place with regard to the wider audit environment. • Annual reviews of the Internal Audit function at North Herts have not highlighted any significant issues in relation to the CIPFA Code of Practice for Internal Audit. It will be vital that this is continued with the introduction of the Shared Internal Audit Service (SIAS), a partnership of six Hertfordshire councils • The shared service is anticipated to reduce the daily rate of audit from £271 to £240. • It is anticipated that that sharing services will increase resilience in internal audit and give a greater economy of scale to allow for access to specialist audit skills. • Oversight of the SIAS will be through a joint officer board of participating Chief Financial Officers which will meet on a quarterly basis and monitor the performance of SIAS to ensure that it delivers the standards and expectations set out in the partnership agreement. The Council will need to ensure that the move to a shared service arrangement has not had a detrimental effect on the quality and scope of the service being provided. • Whilst the partners will jointly oversee the performance of SIAS as a whole, the responsibility for the adequacy of the whole system of internal audit will remain with the Council who will continue to be responsible for overseeing the effectiveness of the internal audit function and be responsible for the effectiveness of governance, risk management and control arrangements.	Green

Internal and external assurances

Area of focus	Summary observations	High level risk assessment
External audit arrangements and programme of activities	• The most recent VfM conclusion confirmed that the Council made proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2010. • Work around the VfM opinion over previous years has also highlighted improvements in performance across the Council, in particular in relation to Managing Finances and Governing the Business.. • The Council has always included management responses to recommendations raised in previous audit reports and have made good progress in implementing these recommendations.	Green