North Hertfordshire District Council

Review of the Council's arrangements for ensuring Value For Money

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October 2012

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Section 1 Executive summary

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Introduction

Value for money conclusion

The Code of Audit Practice 2010 (the Code) describes the Council's responsibilities to put in place proper arrangements to:

- secure economy, efficiency and effectiveness in its use of resources;
- ensure proper stewardship and governance; and
- review regularly the adequacy and effectiveness of these arrangements.

We are required to give our conclusion based on the following two criteria specified by the Audit Commission:

The Council has proper arrangements in place for securing financial resilience

The Council has robust systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.

The Council has proper arrangements for challenging how it secures economy, efficiency and effectiveness

The Council is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.

Financial Resilience 2010/11

Last year we undertook a detailed review which considered the Council's arrangements against the three expected characteristics of proper arrangements as defined by the Audit Commission:

- Strategic financial planning;
- Financial governance; and
- Financial control

This was further supplemented by consideration of a set of key indicators of performance.

The results of the 2010/11 work against these areas were rated on a red / amber / green basis (RAG rated), the results of which have been summarised within the table below.

Area of review	RAG rating
Key indicators of performance	● Green
Strategic financial planning	● Green
Financial governance	● Green
Financial control	● Green

Definitions:

Green	**no causes for concern** - adequate arrangements identified and characteristics of good practice appear to be in place.
Amber	**potential risks and/or weaknesses in this area** - adequate arrangements and characteristics are in place in some areas, but not all, evidence that action is being taken to address known issues
Red	**high risk area** - arrangements are generally inadequate and no clear evidence that action is being taken to address known issue

Financial Resilience 2011/12

Programme of work for 2011/12

To support our conclusions against the Code criteria for 2011/12 we have undertaken a follow up review to the detailed findings to our work performed in the prior year where the Council was either rated as 'Amber', or where the Council's own arrangements are considered to have changed significantly and therefore require to be reassessed. For consistency we have also considered the Council's current performance against the same series of key performance indicators as used in the prior year and followed up on the status of the recommendations that were raised in our prior year report (further details are set out in section 5).

Our 2011/12 programme of work therefore considers the following areas:

Key performance indicators

Strategic financial planning

- The adequacy of planning assumptions within the medium term financial strategy (MTFS); and
- Responsiveness of the MTFS;

Financial control

- Performance management of savings plans

As there were no individual amber ratings within Financial Governance in the prior year and there have been no significant changes to the Council's own arrangements, no detailed review work was considered to be required in this area for 2011/12.

For information, the full list of detailed indicators which are used to form the basis of our assessment of the 'expected characteristics of proper arrangements' are set out in Appendix A.

Key findings

The summary level results of our 2011/12 review are presented below. Detailed ratings against individual indicators are set out in sections 2, 3 and 4.

Key performance indicators ● Green

The Council has demonstrated strong performance against budget in recent years, maintaining the majority of its indicators despite considerable financial pressures. Borrowing will remain an area of ongoing consideration for the Council, in particular when more certainty is known regarding proposed changes to local government funding mechanisms from 2013/14 onwards.

Strategic financial planning ● Green

Our review of the annual budget setting process and development and approval of the MTFS supports that the key assumptions made in setting the budget are consistent with nationally expected levels where appropriate and include an appropriate consideration of income generating activities, industry based expectations regarding inflationary movements and separate savings plan levels.

Review of the process for setting the MTFS also supports that the Council has explored suitable alternatives for options, with an appropriate consideration of both upsides and downsides against a likelihood of achieving calculated values and key risks. Review of in-year monitoring supports that variances are actively managed with a degree of consideration also given to potential mitigation.

Financial control ● Green

Review of the established process in place for preparing the annual savings programme supports that potential efficiencies are suitably identified with an appropriate consideration given to their potential achievement. The Councils achievement of savings plans to date have been good, with a clear emphasis on the embedding of savings in order to ensure ongoing efficiencies.

Financial Resilience 2011/12 (continued)

Overall conclusion

On the basis of our work, having regard to the guidance on the specified criteria published by the Audit Commission, we were satisfied that in all significant respects the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2012.

The way forward

Matters arising from the review of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources have been discussed with the Strategic Director of Finance, Policy and Governance. There were no recommendations arising from our 2011/12 review.

Acknowledgement

We would like to take this opportunity to record our appreciation for the assistance provided by Council staff during our review.

Grant Thornton UK LLP
October 2012

Section 2 Key indicators of performance

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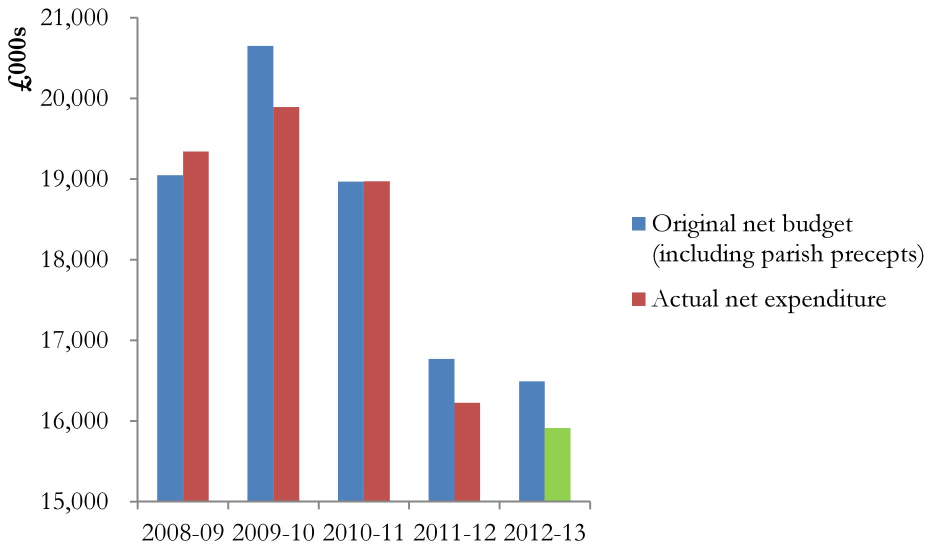
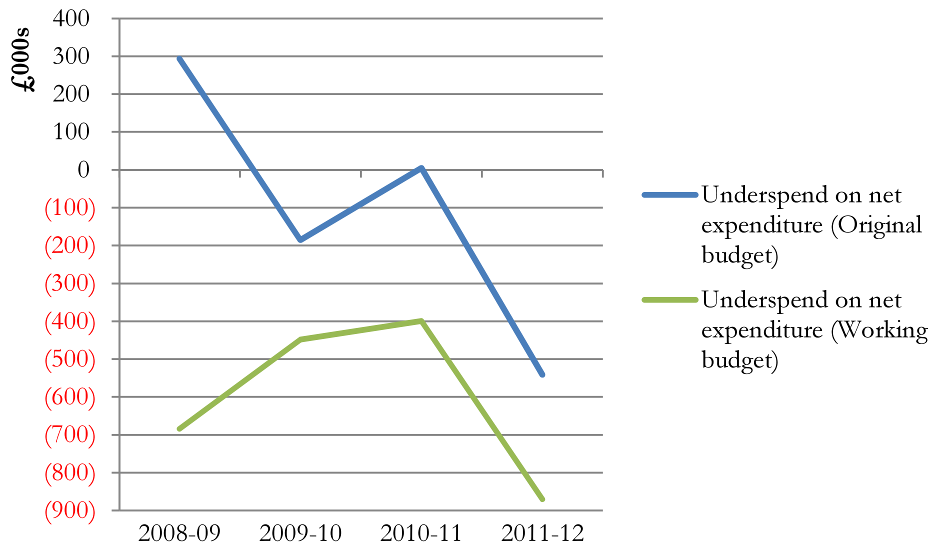
Key indicators of performance

Performance against budget ● Green

- The Council has established a good track record of delivering net expenditure against it's original budget, with significant underspends achieved in the last two years, with an equivalent underspend of £579k forecast for 2011/13. This is highlighted in the graph below:



- The outturn for 2011/12 and forecast position for 2012/13 support that the Council has performed well in accommodating the significant reductions in local authority expenditure required by the outcome of the 2010 Spending Review. The Spending Review represents one of the largest planned reductions in public sector spending since the 1920's, with revenue funding to local government expected to reduce by 26% over a four year period The forecast position for 2012/13 would represent an accompanying 16% reduction in the Council's own net expenditure since 2010/11.



- The graph above highlights the Council's reported underspends against its original and final working budget. The working budget reflects the approval of changes to the original budget from the date that it is originally set in January-February, both for changes in circumstances identified before 1 April, and based on the results of quarterly performance monitoring of individual variances throughout the year.

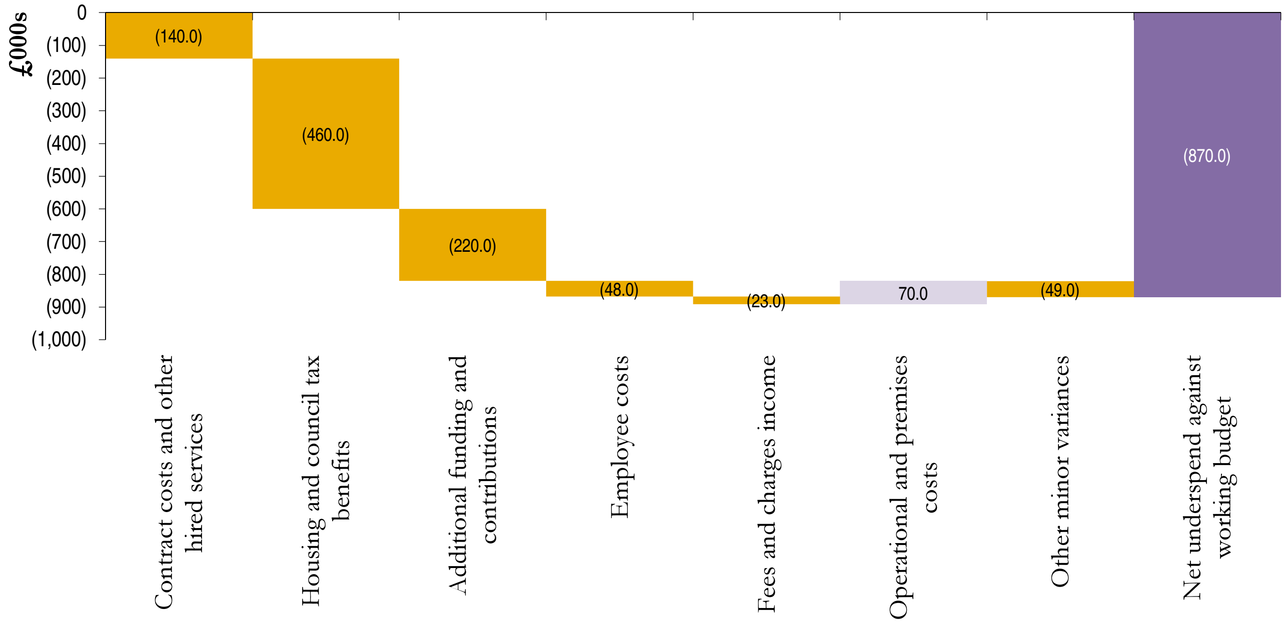
- In addition to the practice of creating and reapproving a working budget throughout the financial year, requests for the 'carry forward' of budgets are also made. The carry forward requests approved in the final quarter of the last 3 years are as follows:

2009/10:	£498k
2010/11:	£290k
2011/12:	£418k

Key indicators of performance (continued)

Performance against budget (continued) ● Green

- A waterfall graph highlighting the major 4th quarter variances against the final 2011/12 working budget is shown below:



- The total annual net variance for housing and council tax benefits is a surplus of £580k. This position is a combination of factors, primarily improvements in the recovery of overpayments, that resulted in a significant improvement against the mid-year subsidy estimate. As such, this variance may be considered likely to be non-recurrent in nature, as the improvements to working practices are likely to result in lower overpayments made to claimants in the first instance and a resulting overall recovery position that is much closer to subsidy estimates in future.
- It should be noted that a number of underspends against budget can reflect corresponding under-delivery of some services. For example, a total of 346 audit days were delivered in 2011/12 against an expected 404 days, with a review of the original annual audit plan during the year having resulted in the cancellation of 7 planned audits. The Council will need to be able to clearly demonstrate that where such under-delivery occurs, there is not a corresponding reduction in the planned scope or quality of services, or increase in risk to the Council's finance or governance arrangements.

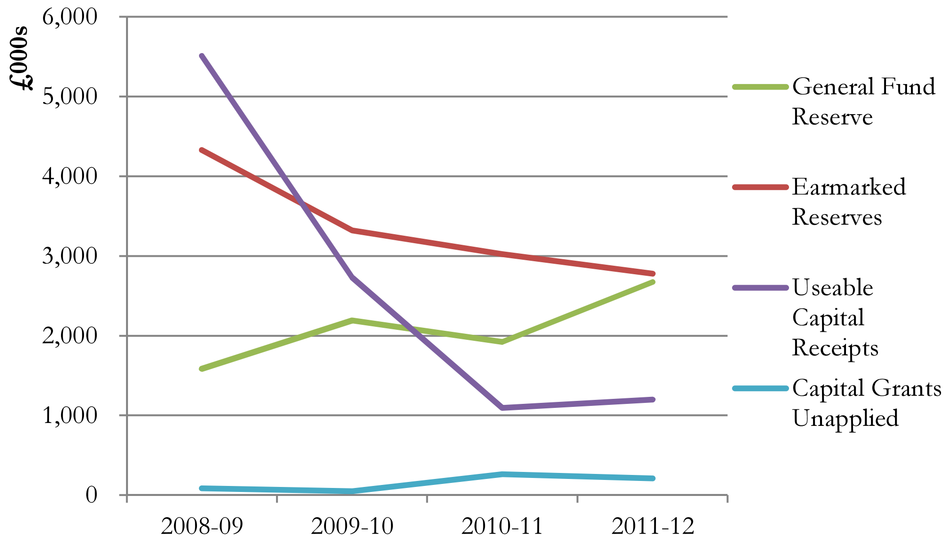
Key indicators of performance (continued)

Reserve balances ● Green

- For several years the Council has adopted a policy of maintaining a minimum General Fund balance of 5% of net expenditure, plus an allowance for identified risks. In real terms, due to following the practice of adopting a working budget throughout the year, the Council has maintained it's General Fund balance significantly above this level, a position that has become more pronounced with the recent reductions in the annual budget.

- A Special Reserve is also maintained, within Earmarked Reserves, for additional financial pressures such as pump priming for initiatives for shared services, changes in working practice, major contract renewals and unexpected contract variation. The balance of this reserve as at 31 March 2012 was £967k.

(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)



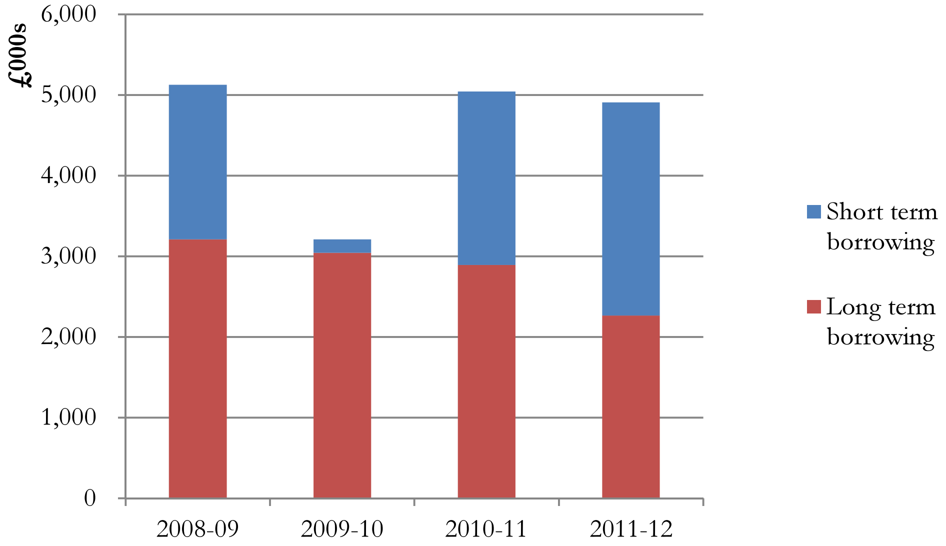
- The overall balance of the Council's reserves has changed significantly in recent years to reflect changes adopted as part of the international code of accounting practices, a significant relative downturn in usable capital receipts from the sale of properties and the dramatic change in local government funding as a result of the 2010 Spending Review.

- The significance of maintaining sufficient General Fund balances is expected to increase over the next 2-3 years due to the announced changes to the administration of housing and council tax benefit, resulting from the Welfare Reform Bill and introduction of Universal Credit, general reductions in non-specific grant funding and the Government decision to localise business rates.

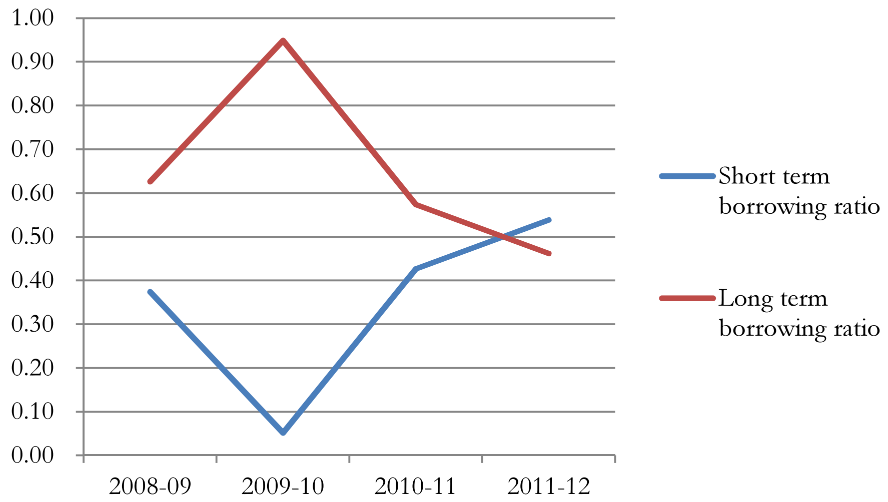
Key indicators of performance (continued)

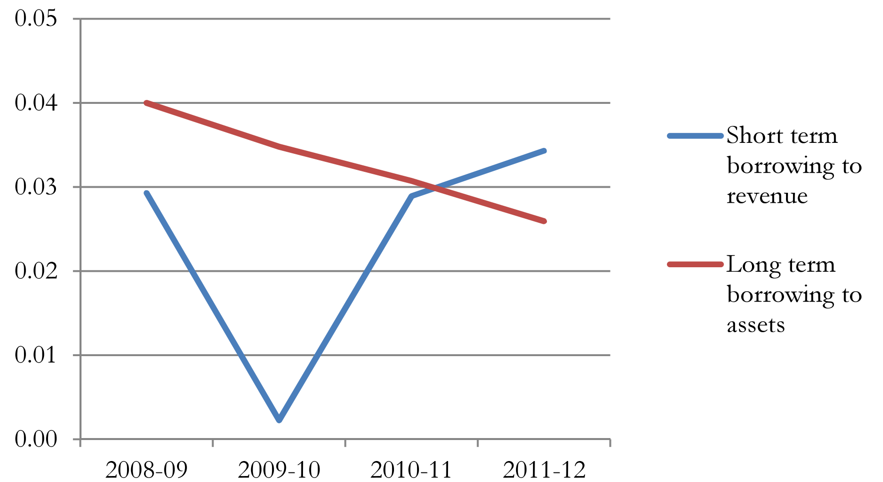
Borrowing ● Amber

- The current overall level of borrowing indicates a reasonably resilient position for the Council and is well within the Council's own prudential limits, however, it can be seen that ratio of short-term to long-term assets has now reversed. Such a movement may indicate a change in emphasis from long-term investment in infrastructure to a shorter-term focus on current resource demands and service delivery, a movement that would be entirely consistent with the impact of the changes brought about by the 2010 Spending Review.



- As historic long-term borrowing moves closer to full repayment the Council is likely to require to comprehensively revisit it's overall Treasury Management strategy, once more certainty is known regarding ongoing changes to local government funding arrangements from 2013/14 onwards.



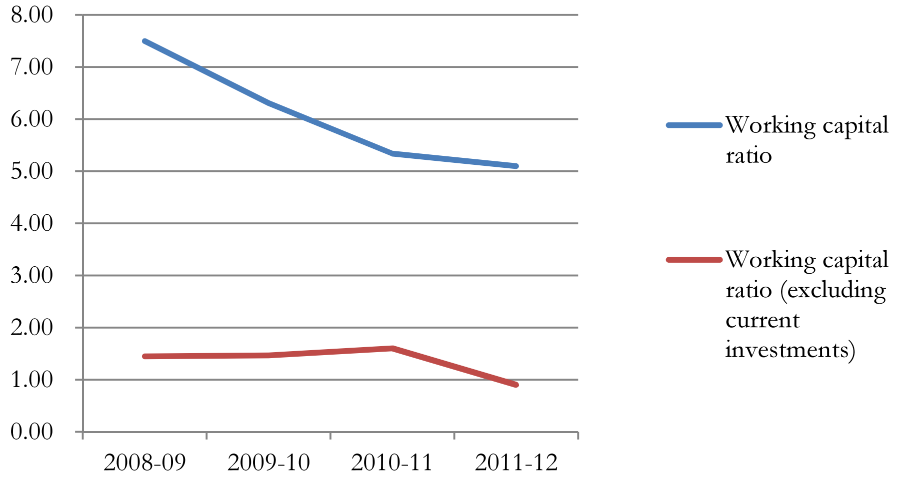


Key indicators of performance (continued)

Liquidity ● Green

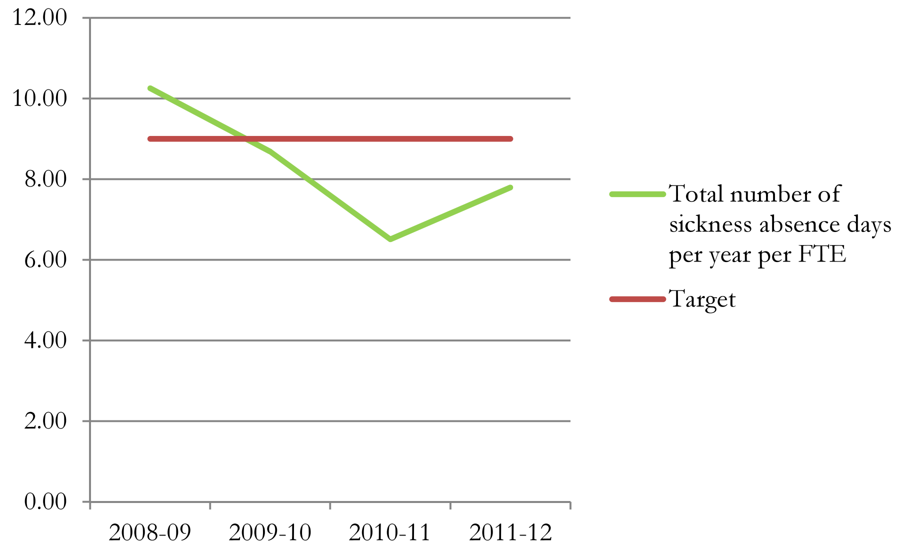
- The working capital ratio indicates whether an entity has enough current assets, or resources, to cover it's immediate liabilities i.e. those over the next twelve month period. As shown in the graph below, the Council's working capital ratio has fallen over the last four years.

- This indicates that the Council's liquidity is decreasing. A ratio of assets to liabilities of 2:1 is usually considered to be acceptable, whilst the Council continues to have a ratio just over 5:1. In general, a high working capital ratio is not considered to be ideal, as it tends to indicate that an entity is not investing excess cash effectively. However, where the Council has invested cash in the form of short-term investments these may have a distorting effect. Were these investments to be excluded from the calculation a revised ratio would be 0.9:1. Such a level is likely to be indicative of a degree of reliance on short-term borrowing to meet fluctuations in resource requirements.



Workforce ● Green

- The Council's sickness absence levels have been showing a consistent reducing trend until recently, although performance remains ahead of the 9 day target, despite an increase in long-term sickness absence. By way of comparison, some studies suggest an overall average public sector rate of 9.6 days and private sector rates between 4.5-6.6 days, depending on the source of figures and the exact calculation applied. The Council may wish to consider reducing it's target accordingly.



- Reducing absenteeism saves money, improves productivity and can have a positive customer service benefit. Absence management is expected to be a particular challenge for all local authorities going forward, given the context of significant pressures on staff to deliver 'more for less' and dramatic changes to the many of local governments historic priorities and responsibilities.

Section 3 Strategic financial planning

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Strategic financial planning

Adequacy of planning assumptions ● Green

- The Council's Medium Term Financial Strategy (MTFS) for the period 2012-17 was adopted by full Council on 8 September 2011 following recommendation by Cabinet.
- Planning assumptions take into account separate expected inflationary increases in pay expenditure, superannuation contributions, falls in interest rates on investments, and contract inflation in accordance with individual contract terms. The rate quoted are consistent with those applied nationally.
- 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, as expected in late 2011*

  ** NB. the final announcement has since been deferred to late 2012*
- A consideration of benchmarking is routinely used to determine the adequacy of assumptions on fees and charges where there is a degree of local discretion and for rates to be competitive with neighbouring councils.
- The final section of the current MTFS highlights key risks and presents alternative scenarios regarding the future uncertainty in relation to the amount of government funding , including anticipated changes such as additional New Homes Bonus income, and the impact that this could have on planned efficiency targets.

Responsiveness of the strategy ● Green

- 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 has been routinely updated each year as part of the annual Corporate Business Planning cycle, whilst also .being subject to non-routine revisits as soon as any additional certainty has been gained in relation to the key risks identified and future government funding plans.
- 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 the need to identify and achieve further savings. The MTFS highlights to members to respective quantified impacts of a 0.5% reduction in interest rates and a 1% increase in council tax (although the Council continues to apply a freeze on council tax increases due to associate government funding incentives).
- In year monitoring reports are considered monthly by corporate management team and submitted quarterly to the Finance, Audit and Risk 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 2011/12 monitoring suggests that effective monitoring, reporting and escalation has occurred in year.

Section 4 Financial control

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Financial control

Performance against savings plans ● Green

- As part of the now established annual cycle, final efficiency plans for are agreed as part of the annual revenue budget at the Cabinet meeting in January, to be recommended to Members for approval as part of the General Fund estimates in February. Draft plans are presented to Cabinet in December following discussion at Member workshops and Area Committees in November and December. Committee minutes and in year papers support an ongoing consideration and revisiting of efficiency targets whenever greater certainty is achieved on future funding from government announcements.

- Individual efficiency proposals identify the link to the Council's priorities as 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. Initial efficiency proposals have been removed by Members in a number of instances where it was felt that there may be an unacceptable impact to the delivery of services, with investigations then carried out to identify other potential options

- In year monitoring reports are considered monthly by corporate management team and submitted quarterly to the Finance, Audit and Risk Committee and Cabinet itself. Specific reporting is included regarding the Red/Amber/Green (RAG) status of Key Corporate 'Health' Indicators and efficiency proposals, with additional detail provided for variances to date against budgets at red or amber status. A review of 2011/12 and first quarter 2012/13 monitoring suggests that effective monitoring, reporting and escalation procedures are in place and are operating effectively.

- Overall performance against budget suggests that the Council has a good track record of delivering savings and embedding efficiencies. The inclusion of 'Achievement of Savings' within the executive summary and detailed results of quarterly monitoring and outturn reporting now allows members to directly assess the achievement against efficiency plans.

- Of the £1,913k of expenditure reduction and income generation proposals agreed in the 2011/12 original budget, £1,660k (87%) was achieved in 2011/12. £151k of the remaining £253k relates to staff restructuring where savings have now been achieved going forward, but were not achieved within the financial year due to the timing of formal approvals and consultation periods.

- Of the £609k of efficiency proposals agreed in the 2012/13 original budget £602k (99%) are expected to be achieved in 2012/13, in part due to £360k of these savings already having been embedded at the time of setting the 2012/13 budget.

- The Council's MTFS emphasises that the more ongoing efficiencies that can be achieved early, the easier it will be to maintain the required level of resources in later years. It is anticipated that some of the efficiencies in future years will be achieved from work currently progressing on looking at alternative means of working, including the potential for shared working with East Hertfordshire and Stevenage Councils, whilst there remains the strong possibility that services may need to be reduced in future should sufficient efficiencies not be forthcoming from these initiatives.

Section 5 Follow up to 2010/11 recommendations

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2010/11 Financial Resilience review recommendations

The 2010/11 Financial Resilience review highlighted four recommendations. The table below provides detail of the progress made:

Area of Review	Recommendation	Responsibility	Timescale	Update	RAG rating
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	See updated review of key performance indicators in section 2. Whilst a direct reference is made to cash flow forecasting within the Treasury Management strategy, with separate treasury management monitoring now made to the Finance, Audit and Risk Committee on a quarterly basis, a profiled cash forecast is not included. With the forthcoming reductions and restructuring to local government funding it is recommended that further consideration be given to introducing this form of monitoring.	● Amber
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 to a 0.5% change in interest rates equating to a potential £200k change in income and considers the fluctuation in rate as part of key risks. Separate treasury management monitoring is now provided to the Finance, Audit and Risk Committee on a quarterly basis.	● Green

2010/11 Financial Resilience review recommendations (continued)

Area of Review	Recommendation	Responsibility	Timescale	Update	RAG rating
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	Ongoing	Three papers were deferred from the June 2011 meeting, including the reported outturn of the 2010/11 revenue and capital budgets, which were therefore received to Cabinet without prior scrutiny. However, no papers were deferred from subsequent meetings and all meetings held in year achieved a quorum, with only three instances identified where members did not ensure the attendance by a suitable substitute member in their absence. No concerns were noted in the report of the Head of Finance, Performance and Asset Management entitled 'The effectiveness of the Finance, Audit and Risk Committee' submitted to the 18 June 2012 committee meeting.	● Green
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	Regular performance updates against the annual plan have been provided to the Finance, Audit and Risk Committee throughout the year. An annual report was provided to the 18 June 2012 committee alongside the annual opinion. A total of 346 audit days have been used during the year rather than the 407 included in the original annual plan. A review of the audit plan during the year resulted in the cancellation of 7 planned audits. The process of setting the annual plan should be kept under review to ensure that an appropriate risk based plan is established and that it can respond to the needs of the Council as they arise during the year.	● Amber

Appendix A Key indicators of 'expected characteristics of proper arrangements'

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Strategic financial planning

Key indicators of good strategic financial planning

In conducting our review of strategic financial planning we have assessed the Council's performance against the following indicators:

- Focus on achievement of corporate priorities is evident through the financial planning process. The MTFS focuses resources on priorities.
- 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 CSR.
- 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.

Financial governance

Key indicators of effective financial governance

In conducting our review of financial governance we have assessed the Council's performance against the following indicators:

Understanding

- 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.
  - Officers and managers understand the financial implications of current and alternative policies, programmes and activities.

Engagement

- There is engagement with stakeholders including budget consultations.

Monitoring and review

- There are comprehensive policies and procedures in place for Members, Officers and budget holders which clearly outline responsibilities.
- 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).

Financial control

Key indicators of effective financial control

In conducting our review of financial control we have assessed the Council's performance against the following indicators:

Budget setting and budget monitoring

- Budgets are robust and prepared in a timely fashion.
- 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.

Finance Department

- The capacity and capability of the Finance Department is fit for purpose.

Financial Systems

- Key financial systems have received satisfactory reports from internal and external audit.
- Financial systems are adequate for future needs.

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.