

<b>Item No:</b> 9.	<b>Classification:</b> Open	<b>Date:</b> 12 September 2018	<b>Meeting Name:</b> Audit, Governance and Standards Committee
<b>Report title:</b>		Budget challenge and governance	
<b>Wards or Groups affected:</b>		All	
<b>From:</b>		Strategic Director of Finance and Governance	

## RECOMMENDATIONS

1. That the audit, governance and standards committee consider the governance arrangements with regard to budget setting and monitoring as set out in this report.

## KEY ISSUES FOR CONSIDERATION

2. Local authorities are required by law to have a balanced budget. To avoid an unbalanced budget local authorities have to be financially resilient. Good financial management is fundamental in establishing confidence in the budget and ensuring that the finances can withstand unexpected pressures. Setting a clear medium-term financial plan will help clarify expected income and expenditure and regular monitoring will ensure that any financial issues are identified early and measures can be brought in to realign the budget. These plans must incorporate any financial, operational and strategic risks faced by the authority.
3. The unprecedented financial challenges facing local councils in recent years, as exemplified by the financial issues at Northamptonshire County Council, who have issued successive section 114 notices, have increased concerns nationally about the financial resilience and sustainability of local authority finances.
4. The Chartered Institute of Public Finance Accountants (CIPFA) believes that in the current financial climate there is a need for appropriate and robust independent challenge and support for some councils on financial strategy and trajectories. Accordingly they are consulting on a new resilience index which is intended to provide challenge where needed so that appropriate action can be taken at a local level to address issues and risks.
5. The following paragraphs provide an overview of the council's general fund revenue budget setting and monitoring arrangements in terms of:
  - Statutory requirements
  - Southwark Constitution and Financial Standing Orders
  - Budget Setting arrangements
  - Budget Monitoring arrangements
  - Role of Audit.

### Statutory arrangements

6. The council has a legal obligation to set a balanced budget on an annual basis as prescribed in the Local Government and Finance Act 1992 and associated

Regulations and to set the level of council tax for the forthcoming financial year. The deadline by which all council's must set a balanced budget is the 11 March each year.

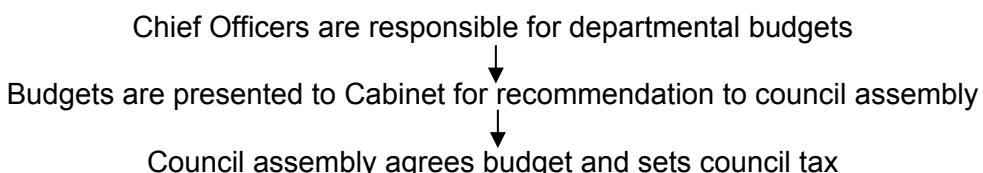
7. Section 25 of the Local Government Act 2003 requires the chief finance officer (strategic director of finance and governance) to report to the authority on (a) the robustness of the estimates made for the calculation of the revenue budget, and (b) the adequacy of the proposed financial reserves. The authority is required to have regard to the chief financial officer's report when setting the level of council tax.

### **The section 151 officer**

8. The strategic director of finance and governance is the Council's responsible officer under section 151 of the local government act 1972, and part VIII of the local government finance act 1988, for the proper administration of its financial affairs. This means that the section 151 officer is legally responsible for ensuring that the council manages its finances properly.
9. The section 151 officer has very specific legal responsibilities to the local tax payer. The role and responsibilities were developed by case law where it was established that the treasurer (section 151 officer) is not merely a servant of the council, but holds a fiduciary responsibility to local tax payers. This means that when s151 officers give advice and carry out their jobs they have to think about what is the best decision not only for the council, but also for local tax payers.
10. The s151 officer has a number of powers to support this responsibility. If the s151 officer judges that the council is unable to set or maintain a balanced budget they must consider the possibility of a Section 114 notice. Such a notice is only given in the gravest of circumstances. The process is governed under legislation and once issued the council has 21 days to consider a response. However, during that time spending and other financial activity is suspended.

### **Southwark constitution and financial standing orders**

11. The constitution reserves a number of decisions to Council Assembly, including agreeing the budget and determining the level of local taxation. The budget includes the allocation of financial resources to different services and projects, proposed contingency funds including reserves and balances; setting the council tax; decisions relating to the control of the council's borrowing requirement; the treasury management strategy and the setting of virement limits.
12. The budget and policy framework procedure rules state that the council will be responsible for the adoption of the budget and policy framework. Once the framework is in place, it will be the responsibility of the cabinet to implement it within the resources approved by council. The process by which the budget and policy framework shall be developed is summarised below:



13. The constitution sets out the responsibilities for Overview and Scrutiny Committee (OSC) with regard to examining and monitoring the performance of services

provided by the council and other agencies. OSC has specific responsibility for scrutinising matters in respect of the policy and budget framework.

14. The constitution also contains the financial standing orders (FSOs) which provide the framework for managing the council's affairs.
15. The strategic director of finance and governance and strategic directors have clear specific roles to play in budget preparation and monitoring which are defined in FSOs.
16. The strategic director of finance and governance is the officer appointed by the council in accordance with Section 151 of the Local Government Act 1972. All matters connected with the financial administration of the council's affairs are the delegated responsibility of the strategic director of finance and governance, except any matters that are delegated or reserved.
17. Strategic directors are responsible for:
  - preparing the revenue budget for the services in his/her departments in consultation with the relevant member of the cabinet, which will have regard to the community strategy, corporate plan, corporate priorities and business plans.
  - ensuring that resources are allocated through a detailed budget on SAP by the deadline set by the chief finance officer.
  - ensuring that reports are submitted to the relevant cabinet member(s),
  - seeking approval of fees and charges in relation to their areas of responsibility.
18. FSOs also include the following sections relating to the budget:
  - Preparation of the revenue budget
  - Setting the annual budget and council tax
  - Monitoring and control of the revenue budget

#### **Revenue budget setting arrangements: an overview**

19. The revenue budget is the term used to describe the amount that the council spends on its day-to-day running of services. This includes wages and salaries, property and transport running costs and payments to suppliers. In addition to the running costs of services, councils have to fund the costs of borrowing money to pay for their capital assets.
20. Once all these things are taken into account, along with specific grants and fees and charges, a figure known as net revenue expenditure is reached. From the net revenue expenditure figure any use of council reserves is subtracted to get to a budget requirement figure that is then funded from general government grant, non-domestic rates and council tax.
21. Objectives of the budget setting process:
  - To set a balanced budget and to set council tax by the statutory deadline
  - To give financial expression to the fairer futures council plan for service delivery in the coming year
  - To make a detailed allocation of available financial resources
  - To set a target against which performance may be monitored

- To provide authority for officers to incur expenditure within the framework of financial regulations, standing orders and the scheme of delegation.
  - To ensure that proper financial control is being exercised.
22. In September 2016, the cabinet approved the Fairer Future Medium Term Financial Strategy (FFMTFS) and Integrated Efficiency Plan noting the relationship to the Council Plan and the theme to be fit for the future (Appendix A). The FFMTFS sets out the financial principles of the council and the remit within which it plans its business. The strategy is set in the context of a number of key themes, each structured to support all major policy objectives and priorities as set out in the council plan. These themes are closely linked to the Fairer Future for all vision and the values and promises linked to it. The refreshed council plan approved by Cabinet in July will be presented to council assembly in November.
23. Equalities impact assessments are undertaken on all budget proposals.

### **2019-20 budget setting process**

24. The following table provides an overview of the 2019-20 budget setting timetable

Date	Task
February 2018	2018-19 budget approved by council assembly
June/July 2018	<p>The 2019-20 budget is developed from the 2018-19 base budget.</p> <p>The base budget is updated for latest assumptions of:</p> <ul style="list-style-type: none"> <li>• resource availability - government funding, retained business rates, council tax, fees and charges. Funding risk is increasingly being transferred to council as most resources generated locally.</li> <li>• unavoidable budget pressures, e.g. inflation, debt financing, government policy changes etc.</li> </ul> <p>At this stage no growth has been assumed, e.g. manifesto commitments, demand etc.</p> <p>The difference between available resources and base budget indicates an initial budget gap</p>
July 2018	Informal Cabinet considered the budget assumptions and agreed next steps and framework for budget discussions to be undertaken during the summer ahead of the budget challenge sessions
August 2018	Budget guidance issued by strategic director of finance and governance
September 2018	Financial Remit report considered by Cabinet
September 2018	Budget challenge and scrutiny sessions commence.
November 2018	Cabinet update on budget
December 2018	Provisional Local Government Finance Settlement
December 2018	OSC agree budget scrutiny
December 2018	Council tax base report approved by Cabinet
December 2018	Draft budget proposals considered by Cabinet
January 2019	Finalised budget proposals considered by Cabinet

January 2019	Budget scrutiny meetings
January 2019	Fees and charges reports agreed by portfolio holders
January 2019	Final Local Government Finance Settlement
January 2019	Group meetings/briefings/consultation
February 2019	Final budgets are presented to Cabinet for approval and recommendation to council assembly
February 2019	Council Assembly approves budget and set council tax
March 2019	Budgets loaded on SAP and budget responsibilities agreed by strategic directors

25. A key element of the budget process is the Budget Challenge Panels. At these sessions Strategic Directors will present their budget options at challenge panels comprising relevant cabinet members, chief executive, strategic director of finance, supporting chief officers and departmental finance managers.
26. The remit of the sessions is to present targeted savings on the net budget. The target being set at slightly above the required level of savings identified in the budget remit report in recognition that some proposals will not be acceptable or may be scaled down as we move through the programme or even moved into future years.
27. The sessions will consider:
- Overview of 2017-18 outturn and 2018-19 updated current forecast (including progress on agreed 2018-19 budget savings targets);
  - Review of 2019-20 saving proposals as set out in schedules including fees and charges;
  - Review of 2019-20 commitments, including the cost of any manifesto commitments;
  - Review the separate higher risk savings options;
  - Beyond 2019-20 – early thoughts on future pressures and opportunities.
28. Budget proposals will consist of:
- Growth and commitments:
- New commitments and growth bids will only be considered where there is full evidence to support any bid, including demonstration that current costs for the service are no higher than average for comparable authorities.
  - All growth bids put forward will be reviewed through the budget planning process using information provided on the proformas issued as part of the budget planning guidance. Where the business case put forward is either insufficient or unjustified it will be returned and not included in estimates.
  - Any resources required to achieve savings proposed (e.g. redundancy costs) will need to be identified in full separately as commitments, not netted off against planned savings and clearly cross referenced to the savings option.
  - Fall-out of grant should also be treated as growth, business cases continued funding should also include the current exit strategy.
  - Growth can only be proposed and considered if matched by additional savings and efficiencies over that required by the financial remit.
- Efficiencies and other savings
- a schedule of efficiency and other savings options to close the departmental budget gap

- benchmarking and comparison with others will be used to review high cost services
- invest to save will be considered on the basis of sound and robust business cases
- a review of the extent and costs of discretionary services being provided in the context of service priorities and resources available; to set out options for the cessation or reduction of expenditure on these services which are not of a high priority

#### **Fees and charges**

- Corporate policy requires fees and charges are increased to a level, at a minimum, that is equal to the most appropriate London average (e.g. inner London, family, groupings etc.) except where this conflicts with council policy, would lead to adverse revenue implications or would impact adversely on vulnerable clients
  - All fees and charges capped by statute are to be increased to the maximum level the cap allows;
  - External income is maximised and mindful of cost of collection;
  - Increases considered in IDM reports.
29. The outcome of the Budget Challenge Sessions will be the presentation of budget options to Cabinet in November/December.

#### **Capital investment and treasury management**

30. Capital investment and treasury management decisions are fully integrated within the financial planning and budget setting arrangements.
31. Any capital expenditure that is not financed immediately by capital receipts, capital grants or revenue resources will need to be funded by borrowing. The council can temporarily utilise other resources in lieu of external borrowing to fund capital expenditure. This is referred to as internal borrowing and is function of treasury management.
32. In approving the inclusion of schemes and projects within the capital programme, the council ensures all of the capital and investment plans are affordable, prudent and sustainable. In doing so the council will take into account the arrangements for the repayment of debt, through a prudent MRP policy in line with MRP guidance produced by the Ministry of Housing, Communities and Local Government.
33. The capital financing charges, any additional running costs arising from capital investment decisions or additional income from, for example, commercial investments are incorporated within the annual budget and medium term financial plans. This enables members to consider the consequences of capital investment alongside other competing priorities for revenue funding.

#### **Reserves, balances and central contingency**

34. As well as ensuring that sufficient funds are available to finance the ongoing management of the council services, the strategic director of finance and governance needs to be assured that there is an appropriate level of reserves and balances available. The Local Government Act 2003 requires the chief finance officer to report on the adequacy of reserves held, and requires members to have regard to that report in setting the budget. The Act also gives powers to the Secretary of State to specify a minimum of reserves to be held, but those powers have not yet been applied.

35. Maintaining an adequate level of reserves and balances are therefore key factors in the strategic director of finance and governance's assessment of the robustness of the budget. Southwark's relatively low levels of balances and reserves when compared to similar councils in London have been reported to cabinet and more recently to audit, governance and standards committee in the external auditors Audit Findings Report 2017-18.
36. The position remains under close review and the s151 officer will continue to make recommendations as appropriate within the Policy and Resources Strategy.
37. The guiding principles on use of reserves is set out below:
  - to present balanced budgets year on year without recourse to reserves and balances except for specific earmarked projects
  - to maintain a central contingency at a sufficient level to cover demand pressures that are volatile, difficult to predict or unforeseen at the time the budget is set
  - to maintain reserves and balances at a level sufficient to manage the potential risks and opportunities of the organisation.
  - to target an increase in general fund balances to £20m over the course of medium term, in line with similar organisations in London
  - to maintain appropriate earmarked reserves to mitigate risk and smooth cost pressures arising from major council projects and priorities, not least regeneration and development and modernisation and service improvement.

#### **Revenue budget monitoring arrangements: an overview**

38. Following approval by the council of the annual budget, strategic directors may spend within the agreed budget for their departments. They must ensure that the net expenditure for their departments does not exceed the approved budget.
39. Strategic directors must:
  - Ensure there are adequate systems to monitor and audit the resources allocated to their services
  - Monitor at least monthly the projected income and expenditure outturn for the year
  - Present reports to the relevant cabinet member monthly
40. The strategic director of finance and governance will report on the overall financial position to the cabinet on a regular basis.
41. The council's prime financial system is SAP. Budgets are loaded on the system prior to the start of the financial year. Forecast outturn positions are updated monthly.
42. From time to time specific corporate action is required to address demand and spending pressures outside of the routine budget management arrangements. For example, the Council established a Budget Recovery Board in 2017 to help manage the significant pressures within Children's and Adults social care. The Budget Recovery Board provided the necessary support and scrutiny to help realise savings and to ensure services were able to obtain a secure financial footing. The Budget Recovery Board process continues for Children's Services in 2018-19 to ensure a continued budget improvement trajectory.

### **Role of audit**

#### **External audit**

43. External audit provide an important role in ensuring proper stewardship of public money. External auditors look not only at the financial statements but also at the financial aspects of the council is managed. The external auditor must satisfy themselves that the accounts are prepared in accordance with regulations and accounting rules and that the council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

#### **Internal Audit**

44. The council's internal audit service evaluates the effectiveness of the councils risk management control and governance processes. The internal auditors focus their efforts on major areas of risk, including strategic and service risks as well as financial risks. Internal audit will periodically review the procedures for setting and monitoring the budget.

### **Community impact statement**

45. This report is not considered to have a direct impact on local people and communities.

### **Resource implications**

46. There are no direct resource implications in this report.

### **Consultation**

47. There has been no consultation on this report.

### **SUPPLEMENTARY ADVICE FROM OTHER OFFICERS**

48. None required.

### **Reasons for lateness**

49. The report was updated following feedback from consultation between the strategic director of finance and governance and the chair of audit, governance and standards committee.

### **Reasons for urgency**

50. The report sets out the governance procedures for the council's accounts for the committee to consider offering feedback on; and a later meeting would not allow officers time to make any amendments to the process if any were recommended.

### **BACKGROUND DOCUMENTS**

<b>Background Papers</b>	<b>Held at</b>	<b>Contact</b>
Constitution	Council website	Rob Woollatt

## APPENDICES

No.	Title
Appendix A	Fairer Future medium term financial strategy and integrated efficiency plan 2017-18 to 2019-20

## AUDIT TRAIL

<b>Lead Officer</b>	Duncan Whitfield, Strategic Director of Finance and Governance	
<b>Report Author</b>	Rob Woollatt, Interim Departmental Finance Manager	
<b>Version</b>	Final	
<b>Version Date</b>	11 September 2018	
<b>Key Decision</b>	No	
<b>CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / CABINET MEMBER</b>		
<b>Officer Title</b>	<b>Comments sought</b>	<b>Comments included</b>
Director of Law and Democracy	N/A	N/A
Strategic Director of Finance and Governance	N/A	N/A
Cabinet Member	N/A	N/A
<b>Final Report Sent to Constitutional Team</b>	11 September 2018	