

## **Audit Committee**

**28 June 2019**

### **Consideration of 'Going Concern Status' for the Statement of Accounts for the year ended 31 March 2019**

#### **Ordinary Decision**

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## **Report of John Hewitt, Corporate Director of Resources**

### **Electoral division(s) affected:**

Countywide

### **Purpose of the Report**

1. Durham County Council is required to assess whether it should be considered as a 'going concern' organisation, and whether the council's annual accounts should be prepared on that basis. This report considers the council's status as a going concern and recommends that Members approve this.

### **Executive Summary**

2. When preparing the annual statement of accounts the council complies with the Code of Practice on Local Authority Accounting 2018/19 (the Code) as published by the Chartered Institute of Public Finance and Accountancy (CIPFA). The Code requires the accounts to be prepared on a going concern basis.
3. This report details the reasons why it is recommended that the council be considered as a going concern and it is appropriate for the statement of accounts to be prepared on that basis. In summary those reasons are:
  - (a) the financial position of the council remains healthy;
  - (b) as at 31 March 2019 the council held general reserves of £25.1 million and reserves earmarked for specific future

purposes, including those held for schools, of £226.4 million;

- (c) net assets at 31 March 2019 amounted to £428.6 million, an increase of £66.3 million during 2018/19;
- (d) the council has been able to set a balanced budget for 2019/20 and has a clear plan in place to continue to deliver local services up to 2022;
- (e) the council has a history of stable finance and ready access to financial resources in the future; and
- (f) there are no significant financial, operating or other risks that would jeopardise the council's continuing operation.

## **Recommendations**

- 4. It is recommended that:
  - (a) the council be considered as a going concern and therefore
  - (b) the statement of accounts are prepared on that basis.

## **Background**

- 5. The general principles adopted in compiling the statement of accounts are in accordance with the Code. The Code defines proper accounting practices for local authorities in England, Wales, Scotland and Northern Ireland.
- 6. The Code requires that a local authority's statement of accounts is prepared on a going concern basis; that is, the accounts should be prepared on the assumption that the authority will continue in operational existence for the foreseeable future. This means that the Comprehensive Income and Expenditure Statement and Balance Sheet assume no intention to curtail significantly the scale of the operation.
- 7. An inability to apply the going concern concept can have a fundamental impact on the financial statements. In reality, it would be highly unusual for a local authority to have a going concern problem. There may be cases where part of an authority's operations cease to be viable or affordable. However, this will not give rise to a going concern issue for the authority given that the impact would be restricted to only that part of the

operation. Transfers of services under combinations of public sector bodies similarly do not negate the presumption of going concern.

## Key Issues

8. The assumption that a local authority's services will continue to operate for the foreseeable future is made because local authorities carry out functions essential to the local community and are themselves revenue raising bodies (with limits on their revenue raising powers arising only at the discretion of central government). If an authority were in financial difficulty, the prospects are therefore that alternative arrangements might be made by central government either for the continuation of the services it provides or for assistance with the recovery of a deficit over more than one financial year.
9. Local authorities derive their powers from statute and their financing and accounting framework is closely monitored by primary and secondary legislation. It is a fundamental concept of local authority accounting that wherever accounting principles and legislative requirements are in conflict, the legislative requirements then apply.
10. An organisation must consider its financial performance to assess its ability to continue as a going concern. This assessment should cover historical, current and future performance.

## Historical Position

11. The following table shows the net assets of the council for the last five years:

<b>Year ended 31 March</b>	<b>Net Assets £m</b>
2015	466.547
2016	568.129
2017	335.364
2018	362.326
2019	428.605

12. The external auditor provides a 'Value For Money' conclusion at each year end providing their opinion on whether the council has put arrangements in place for securing economy, efficiency and effectiveness in its use of resources. The council's arrangements

are considered against one overall criterion which is made up of three sub criteria as set out by the National Audit Office (NAO).

13. The overall criterion is 'in all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people'. The three sub-criteria are: Informed decision-making; Sustainable resource deployment; and Working with partners and other third parties.
14. The last Audit Completion Report related to 2017/18 and was reported to the Audit Committee on 31 July 2018. Within that report the external auditor stated he was satisfied that in all significant respects, the council had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2018.

### **Current Position**

15. At 31 March 2019 the council held general reserves of £25.1 million and reserves earmarked for specific future purposes, including those held for schools, of £226.4 million.
16. The financial position of the council remains healthy. Net assets at 31 March 2019 amounted to £428.6 million, an increase of £66.3 million during 2018/19. This is mainly due to an increase in the value of property, plant and equipment and short term investments.

### **Future Plans**

17. The council approved its budget for 2019/20 and Medium Term Financial Plan (MTFP 9) to 2022/23 in February 2019.

### **Medium Term Financial Plan (MTFP) 9 – 2019/20 to 2022/23**

18. The financial outlook for the council and the whole of local government remains extremely challenging. The council has faced government funding reductions since 2010/11 and the financial outlook will continue to be extremely uncertain for the foreseeable future as the outcome and timing of the anticipated Fair Funding Review and Comprehensive Spending Review is unknown.
19. It is apparent therefore that the financial landscape for local authorities will continue to be extremely challenging resulting in

the longest period of austerity in modern times. By 31 March 2019 the council had delivered savings of £224 million since 2011, with additional savings of £10.3 million approved for 2019/20. It is forecast that total savings in the period 2011/12 to 2022/23 will be £263 million.

20. The Final Local Government Finance Settlement confirmed a £14.2 million reduction in Revenue Support Grant (RSG) for the Council in 2019/20 as expected.
21. Looking back to MTFP (1) the following drivers for the council's financial strategy were agreed by Cabinet on 28 June 2010, which still underpin the strategy in the latest MTFP(9):
  - (a) To set a balanced budget over the life of the MTFP whilst maintaining modest and sustainable increases in council tax;
  - (b) To fund agreed priorities, ensuring that service and financial planning is fully aligned with the Council Plan;
  - (c) To deliver a programme of planned service reviews designed to keep reductions to front line service to a minimum;
  - (d) To strengthen the council's financial position so that it has sufficient reserves and balances to address any future risks and unforeseen events without jeopardising key services and delivery outcomes;
  - (e) To ensure the council can continue to demonstrate value for money in the delivery of its priorities.
22. Throughout the period covered by the MTFP (1) 2011/12 through to MTFP (9) 2022/23, the cumulative savings required has risen from an originally forecast £123 million to a revised and updated forecast £263 million. It is therefore clear that it will become increasingly difficult to protect frontline services going forward. However, to date, the council has implemented the agreed strategy very effectively.
23. The benefits of delivering savings early if practical to do so, cannot be over emphasised. The utilisation of reserves has been essential in ensuring the smooth delivery of the savings targets and enabled a managed implementation of proposals across financial years.

24. In general, the council has been quite accurate in forecasting the level of savings required, which has allowed the development of strong plans and has enabled the council to robustly manage the implementation and delivery on time, including meeting extensive consultation and communication requirements. This has put the council in as strong a position as possible to meet the ongoing financial challenges across this medium term financial plan and beyond, where savings proposals are becoming more complex and difficult to deliver and will inevitably require increased utilisation of reserves to offset any delays and smooth in reductions across financial years.
25. It is clear that austerity will continue over the three year period of MTFP (9) resulting in at least twelve years of significant funding reductions and the need to identify significant annual savings to balance the budget. This means that the council continues to face a very considerable financial challenge to balance budgets whilst providing a good level of service.
26. After taking into account base budget pressures, additional investment and savings, the council's net budget requirement for 2019/20 is £400.031 million. The financing of the net budget requirement is detailed in the following table.

### Financing of the 2019/20 Budget

Funding Stream	Amount
	<b>£m</b>
Revenue Support Grant	27.620
Business Rates	54.401
Business Rates – Top Up Grant	71.613
Collection Fund Surplus	2.168
Council Tax	222.275
New Homes Bonus	6.709
Section 31 Grant	10.423
Adults/ Childrens Pressures Grant	4.822
<b>TOTAL</b>	<b>400.031</b>

### Capital Funding

27. On 20 February 2019 Council approved the 2018/19 revised capital budget and the MTFP (9) capital budget for the period 2019/20 to 2021/22.
28. Service groupings developed capital bid submissions alongside the development of revenue MTFP (9) proposals. Bids were

submitted in the main for 2019/20 to maintain the two year rolling programme approach to the capital budget. The capital Member Officer Working Group (MOWG) considered the capital bid submissions taking the following into account:

- (a) service grouping assessment of priority;
  - (b) affordability based upon the availability of capital financing. This process takes into account the impact of borrowing on the revenue budget;
  - (c) whether schemes could be self-financing i.e. capital investment would generate either revenue savings or additional income to repay the borrowing costs to fund the schemes.
29. Whilst considering capital bid proposals, MOWG have continued to recognise the benefits of committing to a longer term capital programme to aid effective planning and programming of investment. At the same time, MOWG also recognised the need for caution in committing the council to high levels of prudential borrowing at this stage for future years.
30. The need to continue to invest in capital infrastructure is seen as an essential means of maintaining and regenerating the local economy whilst supporting job creation.

## MTFP (9) Capital Programme

Service Grouping	2018/19	2019/20	2020/21	2021/22 to 2022/23	Total
	£m	£m	£m	£m	£m
Adult and Health Services	0.032	-	-	-	0.032
Children and Young People's Service	18.995	28.757	15.397	0.522	63,671
Regeneration and Local Services	75.792	105.939	91.531	10.147	283,409
Resources	5.037	9.534	5.797	-	20,368
Transformation and Partnerships	3.963	3.769	15.958	-	23,690
<b>TOTAL</b>	<b>103.819</b>	<b>148.000</b>	<b>128.683</b>	<b>10.669</b>	<b>391.171</b>
<b>Financed by:</b>					
Grants & Contributions	65.744	40.034	28.393	0.314	134.485
Revenue & Reserves	24.868	31.262	2.871	0.710	59.710
Capital Receipts	13.206	9.245	10.578	3.760	36.790
Borrowing	-	67.460	86.841	5.885	160.186
<b>TOTAL</b>	<b>103.819</b>	<b>148.000</b>	<b>128.683</b>	<b>10.669</b>	<b>391.171</b>

31. The council has been able to set a balanced budget for 2019/20 and has a clear plan in place to continue to deliver local services up to 2023. Based upon this, it is evident that the council is a going concern.

### Financial Reserves

32. Reserves are held as a:
- (a) working balance to help cushion the impact of any uneven cash flows and avoid unnecessary temporary borrowing – this forms part of the general reserves;
  - (b) contingency to cushion the impact of any unexpected events or emergencies e.g. flooding and other exceptional winter weather - this also forms part of general reserves;
  - (c) means of building up funds, earmarked reserves to meet known or predicted future liabilities.

33. The council's current reserves policy is to:
- (a) set aside sufficient sums in earmarked reserves as is considered prudent;
  - (b) aim to maintain general reserves of between 5% and 7.5% of the net budget requirement in the medium term, which in cash terms is up to £30 million.
34. Based on the level of reserves held, the council has demonstrated robust financial management that underpins its status as a going concern.

### **Risk**

35. The Council has previously recognised that a wide range of financial risks need to be managed and mitigated across the medium term. The risks faced are exacerbated by the outcome of the anticipated Comprehensive Spending Review and Fair Funding Review which will determine the funding available to the council. There is added uncertainty brought about by the expected exit from the European Union. All risks will be assessed continually. Some of the key risks identified include:
- (a) Ensure the achievement of a balanced budget and financial position;
  - (b) Ensure savings plans are risk assessed across a range of factors e.g. impact upon customers, stakeholders, partners and employees;
  - (c) Government funding will be determined by the outcome of the Comprehensive Spending Review and Fair Funding Review; the timing of both are uncertain at present. There is a risk that a deterioration in the public finances could result in further savings targets for local government in excess of those agreed to date;
  - (d) The localisation of council tax support passed the risk for any increase in council tax benefit claimants onto the Council. Activity in this area will need to be monitored carefully with medium term projections developed in relation to estimated volume of claimant numbers;
  - (e) The Council retains 49% of business rates collected locally but is responsible for settling all rating appeals, including any liability prior to 31 March 2013. Increasing business

rate reliefs and appeals settlements continue to make this income stream highly volatile and requires close monitoring to fully understand the implications on the MTFP;

- (f) The impact of future increases in inflationary factors such as the national living wage needs to be closely monitored;
- (g) The council continues to experience increases in demand for social care services. Although some allowance is made for demand increases across the MTFP(9) period, this issue will need to be closely monitored;
- (h) The impact of Brexit which could affect future government finance settlements, inflation and European funding.

36. Based upon the above there are no risks which would indicate that the council is not a going concern.

### **Conclusion**

37. When approving the accounts the Audit Committee Members, being those charged with governance for the council, will need to consider which of the following three basic scenarios is the most appropriate:

- (a) The body is clearly a going concern and it is appropriate for the accounts to be prepared on the going concern basis;
- (b) The body is a going concern but there are uncertainties regarding future issues which should be disclosed in the accounts to ensure the true and fair view;
- (c) The body is not a going concern and the accounts will need to be prepared on an appropriate alternative basis.

38. Based upon the assessment undertaken, in my view:

- (a) The council has a history of stable finance and ready access to financial resources in the future;
- (b) There are no significant financial, operating or other risks that would jeopardise the council's continuing operation.

39. The council is therefore a going concern and it is appropriate for the statement of accounts to be prepared on that basis.

## **Other useful documents**

- (a) County Council – 20 February 2019 – Medium Term Financial Plan, 2019/2 to 2021/22 and Revenue and Capital Budget 2019/20
- (b) County Council – 20 February 2019 – Budget 2019/20. Report under Section 25 of Local Government Act 2003
- (c) Audit Completion Report – 2017/18 – Durham County Council
- (d) Cabinet – 13 March 2019 - Forecast of Revenue and Capital Outturn 2018/19 - Period to 31 December 2018.

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## **Appendix 1: Implications**

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### **Legal Implications**

Compliance with the Accounts and Audit Regulations 2015 and the CIPFA Code of Practice on Local Authority Accounting 2018/19 which is based upon approved accounting standards in England and Wales and constitutes proper accounting practice under the terms of section 21(2) of the Local Government Act 2003.

### **Finance**

The report considers the County Council as a 'going concern'.

### **Consultation**

None.

### **Equality and Diversity / Public Sector Equality Duty**

None.

### **Human Rights**

None.

### **Crime and Disorder**

None.

### **Staffing**

None.

### **Accommodation**

None.

### **Risk**

None.

### **Procurement**

None.