

## **Audit Committee**

**29 June 2020**

### **Consideration of 'Going Concern Status' for the Statement of Accounts for the year ended 31 March 2020**

#### **Ordinary Decision**

---



## **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 2019/20 (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 2020 the council held general reserves of £23.95 million and reserves earmarked for specific future

purposes, including those held for schools, of £216.84 million;

- (c) net assets at 31 March 2020 amounted to £229.81 million;
- (d) the council has been able to set a balanced budget for 2020/21 and has a clear plan in place to continue to deliver local services up to 2023/24;
- (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
- (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 £ million</b>
2016	568.129
2017	335.364
2018	362.326
2019	388.566
2020	229.807

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 2018/19 and was reported to the Audit Committee on 31 July 2019. Within that report the external auditor stated he was satisfied that in all significant respects, the council had proper arrangements in place to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2019.

### **Current Position**

15. At 31 March 2020 the council held general reserves of £23.95 million and reserves earmarked for specific future purposes, including those held for schools, of £216.84 million.

16. The financial position of the council remains healthy. Net assets at 31 March 2020 amounted to £229.8 million, a decrease of £158.8 million during 2019/20. This is mainly due to an increase in the estimated pension liability for employees, calculated by the Pension Fund Actuary, for which statutory arrangements for funding the deficit mean that the financial position of the council remains healthy.

### **Future Plans**

17. The council approved its budget for 2020/21 and Medium Term Financial Plan (MTFP) 10 to 2023/24, in February 2020.

### **Medium Term Financial Plan (10) – 2020/21 to 2023/24**

18. The financial landscape for the council is likely to remain challenging for the foreseeable future. The delay to the Comprehensive Spending Review until the Autumn of 2020 means that there will be little certainty over the council's longer term funding outlook and this will need to be carefully managed as the council considers the recovery actions it needs to take and commit to. In addition, the Fair Funding Review and move to 75% Business Rate Retention have been delayed again with an earliest implementation date of 2022/23.
19. The outcome of these reviews will determine the quantum of funding available to local government and the share available to the council. The added uncertainty brought about by the exit from the European Union will serve to compound these issues. There is a risk that funding reductions may continue beyond this point placing further pressure on the MTFP.
20. The council has continued to effectively manage its resources during a period of increasing cost pressures and a backdrop of many years of government funding reductions. The future funding outlook for the public sector and local government is extremely uncertain and the impact of Covid 19 and the recovery from it will undoubtedly impact on the council and its communities for a number of years.
21. The Covid 19 outbreak will have a significant financial impact on the council in 2020/21 and the recovery take place over a number of years. The financial implications of the council's recovery plan will not be fully understood. The council began to experience the impact of the outbreak in March 2020 when a number of front line service facilities were closed and supplier relief began to be

provided to key contractors. There has been an increase in claims for Local Council Tax Support and an expected reduction in business rate income due to business closures. Consequently, the council will suffer significant reductions in income in 2020/21 and beyond.

22. The council's spending has also significantly increased to cope with the outbreak. Whilst some Covid 19 financial support has been received from government, it is unclear as to the extent to which all of the cost pressures and reductions in income will be reimbursed. This represents a financial risk to the council that will form part of future medium term financial planning.
23. By the end of 2019/20, the council had delivered £234 million of financial savings with additional savings of £8 million approved for 2020/21. It is forecast that total savings for the period 2011/12 to 2023/24 will be £282 million.
24. The council's MTFP for the last eleven years has focussed on protecting front line services as far as possible, prioritising back office efficiencies and reductions in management. As this strategy becomes increasingly more difficult to maintain over time, the council's Transformation Programme was designed to ensure all options were exhausted to protect front line services wherever possible. Nevertheless, front line services will inevitably become progressively impacted over the coming years if funding continues to be restricted.
25. The council continues to have a robust financial standing with sound and continuously improving financial management procedures and processes in place.
26. The council continues to face a range of significant budget pressures including general inflation, cost pressures in the care sector, increases in the number of adults and children needing support and rising levels of need, increases in demand for everyday services as the population grows, and increases in core costs such as wage increases, the national living wage and pension contributions.
27. The MTFP sets out the council's approach to achieving a sustainable budget over the medium term whilst ensuring that all revenue resources are directed towards corporate priorities. The MTFP describes the financial direction of the council over the planning period and outlines the financial pressures it will face.

28. In general, the council has been quite accurate in forecasting the level of savings required, which has allowed the development of strong plans and 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 MTFP 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.
29. After taking into account base budget pressures, additional investment and savings, the council's net budget requirement for 2020/21 is £430.059 million. The financing of the net budget requirement is detailed in the following table.

### Financing of the 2020/21 Budget

Funding Stream	Amount
	<b>£m</b>
Revenue Support Grant	28.070
Business Rates	56.083
Business Rates – Top Up Grant	72.780
Collection Fund Surplus	1.740
Council Tax	234.458
New Homes Bonus	7.563
Section 31 Grant	11.713
Adults/ Childrens Pressures Grant	17.652
<b>TOTAL</b>	<b>430.059</b>

### Capital Funding

30. On 26 February 2020 Council approved the 2019/20 revised capital budget and the MTFP (10) capital budget for the period 2020/21 to 2022/23.
31. Service groupings developed capital bid submissions alongside the development of revenue MTFP (10) proposals. Bids were submitted in the main for 2020/21 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.
32. 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.
33. 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 (10) Capital Programme

Service Grouping	2019/20	2020/21	2021/22	2022/23	Total
	£m	£m	£m	£m	£m
Adult and Health Services	-	-	-	-	-
Children and Young People's Service	20.268	30.960	11.176	-	62.404
Neighbourhoods & Climate Change	31.747	38.008	21.397	-	91.152
Regeneration, Economy & Growth	61.966	116.944	84.616	5.512	269.038
Resources	3.593	13.131	4.245	-	20.969
<b>TOTAL</b>	<b>117.574</b>	<b>199.043</b>	<b>121.434</b>	<b>5.512</b>	<b>443.563</b>
<b>Financed by:</b>					
Grants & Contributions	44.604	48.435	31.077	0.050	124.166
Revenue & Reserves	16.021	34.451	2.257	0.430	53.159
Capital Receipts	10.439	9.913	16.469	-	36.821
Borrowing	46.510	106.244	71.631	5.032	229.417
<b>TOTAL</b>	<b>117.574</b>	<b>199.043</b>	<b>121.434</b>	<b>5.512</b>	<b>443.563</b>

34. The council has been able to set a balanced budget for 2020/21 and has a clear plan in place to continue to deliver local services up to 2024. Based upon this, it is evident that the council is a going concern.

## **Financial Reserves**

35. 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.
36. 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 £32 million.
37. Based on the level of reserves held, the council has demonstrated robust financial management that underpins its status as a going concern.

## **Risk**

38. 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 exit from the European Union and also Covid 19. 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) there is no certainty for the quantum of government funding for local government beyond 2020/21. Given the pressures faced, particularly from social care, it is imperative that the quantum is increased and that a long-term settlement is agreed as part of the expected 2020 Comprehensive Spending Review;
- (d) The outcome of the government's Fair Funding Review could result in significant changes to the distribution of government funding;
- (e) The localisation of council tax support which 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;
- (f) Council retaining 49% of all business rates collected locally but also being responsible for settling all rating appeals including any liability prior to 31 March 2013. Increasing business rate reliefs and the revised 'check and challenge' appeals process continue to make this income stream highly volatile and will require close monitoring to fully understand the implications on the MTFP;
- (g) the impact of future increases in inflationary factors such as the National Living Wage and pay awards which will need to be closely monitored;
- (h) the council continuing to experience increases in demand for social care services. Although some allowance is made for demand increases across the MTFP(10) period this issue will need to be closely monitored;
- (i) the funding position for the High Needs Dedicated Schools Grant. It is hoped that the government fully recognises this pressure as part of the Comprehensive Spending Review;
- (j) The impact of Brexit which could affect future government finance settlements, inflation and European funding.

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

## **Conclusion**

40. 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.
41. 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.
42. 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 – 26 February 2020 – Medium Term Financial Plan, 2020/21 to 2023/24 and Revenue and Capital Budget 2020/21
- (b) County Council – 26 February 2020 – Budget 2020/21 Report under Section 25 of Local Government Act 2003
- (c) Audit Completion Report – 2018/19 – Durham County Council
- (d) Cabinet – 18 March 2020 - Forecast of Revenue and Capital Outturn 2019/20 - Period to 31 December 2019.

---

## **Appendix 1: Implications**

---

### **Legal Implications**

Compliance with the Accounts and Audit Regulations 2015 and the CIPFA Code of Practice on Local Authority Accounting 2019/20 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.

### **Climate Change**

None.

### **Human Rights**

None.

### **Crime and Disorder**

None.

### **Staffing**

None.

### **Accommodation**

None.

### **Risk**

None.

### **Procurement**

None.