Audit Committee

4 April 2013

Consideration of 'Going Concern Status' for the Statement of Accounts for the year ended 31 March 2013

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Purpose of the Report

1. Each year, Durham County Council assesses whether it should be considered a 'going concern', and whether the accounts should be prepared on that basis. This report considers the County Council's status as a going concern and asks Members to agree this.

Background

2. The general principles adopted in compiling the Statement of Accounts are in accordance with the 'Code of Practice on Local Authority Accounting 2012/13' (the Code) as published by the Chartered Institute of Public Finance and Accountancy (CIPFA). The Code defines proper accounting practices for local authorities in England, Wales, Scotland and Northern Ireland.

3. 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.

4. An inability to apply the going concern concept can have a fundamental impact on the financial statements.

5. However, it is highly unusual that a local authority would 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; the impact would be restricted to only that part of the operation.

Key Issues

6. 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.

7. 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 apply.

8. 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

9. Durham County Council became a Unitary Authority on 1 April 2009, bringing together the seven former District Councils in County Durham with the County Council.

10. The assets and liabilities of the former District Councils were transferred to the County Council on 1 April 2009. At that date, the Net Assets of the County Council were £1,240.742m, reducing to £900.094m at 31 March 2010. At 31 March 2011 there was a further decrease to £856,994m.

11. Net assets as at 31 March 2012 were £571.779m.

12. External Audit provide a 'Value For Money' conclusion at each year end which gives their opinion on the County Council in two areas:

    - *Financial Resilience* - The organisation 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; and

    - *Securing economy, efficiency and effectiveness* - The organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.

13. In their Annual Governance Statement for 2011/12, External Audit stated, as evidence of financial resilience:

"The Council understands the financial challenges and risks it faces and has worked hard to deliver a sustainable Medium Term Financial Plan (MTFP) for 2012/13 and beyond and is aware of the challenges ahead.

Senior officers and members provide constructive scrutiny on financial matters and there is an effective Audit Committee in place. The Council has updated its medium term financial plan to reflect the savings required over the next four years. Senior officers receive regular finance reports that provide a clear link between budget, in-year forecasts and the year-end forecast."

"The positive financial out-turn for 2011/12 means the Council has positioned itself well for future challenges. In the short-term, the Council is facing existing challenges of dealing with:

- changes to welfare reform;
- business rates localisation;
- new public health responsibilities from April 2013; and
- the further savings and efficiencies required along with any agreed tri-borough collaboration arrangements.

Members and officers recognise the need to continue to work together to maintain momentum on achieving the wider-reaching changes needed to address the required efficiency savings."

14. In their Annual Governance Statement for 2011/12, External Audit further stated, as evidence of securing economy, efficiency and effectiveness:

"The Council has put proper arrangements in place to challenge how it secures economy, efficiency and effectiveness.

The medium term financial plan (MTFP) covers the four year period 2012/13 to 2015/16.The main objective of the programme is to achieve budget savings of up to £79.3 million by 2015/16 while maintaining focus on its vision and priorities for the county which were developed with partners.

The Council is continuing to ensure that sufficient capacity is provided to deliver the programme effectively. Accurately monitoring savings from these projects will continue be important if budget savings are to be achieved as planned."

Current Position

15. The County Council holds general reserves of £21.874m at 31 March 2012 and reserves earmarked for specific future purposes of £100.425m.

16. The Net Assets of the County Council at 31 March 2012 amounted to £571.779m, a decrease of £299.604m.

17. Current forecasts of the likely position as at 31 March 2013 were reported to Cabinet in March 2013. It is anticipated that the County Council will hold general reserves of £24.653m and reserves earmarked for specific future purposes, including those held for schools will be £96.330m.

18. The Housing Revenue Account (HRA) forms part of the County Council's main accounting statements. General reserves held by the HRA as at 31 March 2012 amounted to £7.821m, and those held for specific purposes were £2.460m.

Future Plans

19. The County Council approved its budget for 2013/14 and Medium Term Financial Plan to 2016/17 in February 2013.

Medium Term Financial Plan (MTFP) – 2013/14 to 2016/17

20. The council has faced unprecedented reductions in Government grants since the 2010 Comprehensive Spending Review (CSR) when the expectation for local government was a 28% cut in Government grant for the period 2011/12 to 2014/15. Since then, the position has deteriorated for local government and in total the council are now forecasting that Government support over the six year period 2011 to 2017 will reduce by £139m. This equates to a 36% reduction in Government support over this period.

21. The council's provisional funding baseline for 2013/14 was announced by the Government on 19 December 2012 with the final settlement being announced on 4 February 2013. The funding baseline for 2013/14 is £249.5m which is £9.1m less than the 2012/13 allocation.

22. After also taking into account estimated base budget pressures and growth in some council priority service areas, the medium term financial plan forecast requires the council to deliver £95m savings between 2013/14 and 2016/17. This is in addition to the £93m of savings that the council has had to make in 2011/12 and 2012/13 to balance its budgets.

23. The total savings therefore for the six year period 2011/12 to 2016/17 are estimated to be £188m with the figure expected to exceed £200m by 2017/18.

24. The 2013/14 budget requires savings of £20.9m to achieve a balanced net revenue budget of £457.814m.

25. The following assumptions have been utilised in developing the MTFP model.

(i) Government grant reductions for the MTFP period have been developed utilising information from both the 2013/14 Local Government Finance Settlement and the December 2012 Autumn Statement. The estimated reductions are as follows:

Forecast Government Grant Reductions

Year	Basis	Grant Reduction
		£m
2014/15	Revenue Support Grant reduction	29.086
2015/16	Net Reduction in all Government Funding	15.600
2016/17	Net Reduction in all Government Funding	9.530

(ii) The following estimates have been included for increased income in 2014/15 to offset the £29.086m (17.4%) reduction in Revenue Support Grant.

Increased Income Forecast for 2014/15

Increased Income	
	2014/15 £m
New Homes Bonus	1.250
New Homes Bonus Top Slice Reimbursement	0.750
Top Up Grant – RPI Increase (3%)	1.785
Business Rate Local Share – RPI Increase (3%)	1.600

(iii) Forecast Pay and Price Inflation levels have taken into account the 1% pay increase cap for 2013/14 and 2014/15. They have also taken into account the continuing high levels of price inflation in the economy with the Consumer Price Index (CPI) currently standing at 2.7% and Retail Price Index (RPI) currently standing at 3.1%. These levels are reflected in the 2013/14 Price Inflation allowance.

Pay and Price Inflation Assumptions

Year	Pay Inflation	Price Inflation
2013/14	1%	2.5%
2014/15	1%	1%
2015/16	1.5%	1.5%
2016/17	1.5%	1.5%

(iv) Continuing budget pressures in relation to Carbon Tax, Employer Pension Contributions, Concessionary Fares, Energy price increases and Adult Services demographic pressures.

(v) Continuing need to support both the current and additional capital programmes.

(vi) Council Tax increases for 2014/15 – 2016/17 are assumed to be 2% per annum.

(vii) There is a need for additional savings to be identified for the 2014/15 – 2016/17 period of £51.3m to achieve a balanced position across the MTFP period.

26. The council will face two new risks in future years which do not presently feature in MTFP modelling as detailed below:

(i) **Variation in Business Rate Local Share Income** – at this stage, the 2013/14 local share income is budgeted for at the baseline level set by the Government in the Start Up Funding Assessment (SUFA). It is expected however that actual income in the future could be higher or lower dependent upon the health of the economy in the county. This will need to be closely monitored for both budgetary control purposes and MTFP planning. Regeneration and Economic Development and Resources are working together to develop a framework which can model the movement of the business rate tax base within the county. If local share income reduces, the council will need to find additional savings to replace the income lost.

(ii) **Localisation of County Tax Support (LCTSS)** – from 2013/14 the council will be responsible for financing the LCTSS. Any variation in benefit claimants will change the levels of council tax income received by the council. This variation will again be linked very closely with the health of the local economy in the county.

27. A balanced MTFP model has been developed after taking into account the assumptions above. The MTFP model is summarised in the following table.

MTFP Summary Position

	2013/14	2014/15	2015/16	2016/17	TOTAL
	£m	£m	£m	£m	£m
Reduction in Resource Base	9.852	19.411	20.445	6.958	56.666
Budget Pressures	11.014	8.455	9.937	8.887	38.293
Savings required	**20.866**	**27.866**	**30.382**	**15.845**	**94.959**
Savings to be identified	**0**	**12.122**	**23.309**	**15.845**	**51.276**

28. Although difficult decisions have needed to be taken in order to balance budgets in 2011/12 and 2012/13, the council continues to be successful in delivering savings against its original budget strategy. Although the 2013/14 budget requires the delivery of further savings of £20.9m, there are a number of key service areas that have been protected and some services where the budget has been increased for the benefit of council tax payers including:

- For the fourth consecutive year, council tax bills for council tax payers will stay the same, should the council accept the Government's Council Tax Freeze Grant of £2m which is the equivalent to the amount of income the council would receive from a 1% council tax increase. Council tax bills will however still go up as the Police and Crime Commissioner has increased their council tax precept by 2% and for those payers living in parished areas should their parish council choose to increase their precept. The Fire authority is proposing a zero increase in council tax.

- Increasing the Adult Social Care budget by £1m in recognition of the increasing demands on the council due to demographic changes and more people becoming dependent upon these services. This is in line with the priorities identified through consultation.

- Protecting all 65,000 households in receipt of council tax benefit under the local council tax support scheme despite a 10% cut in government funding.

- Protecting the highways winter maintenance programme in order to keep our main highways infrastructure open for the public. Again this is in line with public consultation findings.

- A key priority of the capital programme is to stimulate regeneration and job creation across the county. In line with the

Council's key priority to stimulate regeneration and job creation across the county, an additional £3.25m of revenue has been allocated to fund prudential borrowing to invest in new and current capital projects amounting to £159m in 2013/14 with a total programme for the period 2013/14 to 2016/17 of £315m.

29. In December 2012, an extensive consultation process led to over 1,500 people giving their views on how the council has managed spending reductions so far, the impact that the reductions have had to date and ideas for making further reductions in the future.

30. The MTFP agreed by Council in February 2012, identified a range of forecast base budget pressures in 2013/14. Throughout the year, Cabinet has approved updated MTFP reports which have reviewed and updated estimates. The following table details the final forecasted position on the 2013/14 Base Budget pressures:

2013/14 Base Budget Pressures

Pressures	Amount £m
Pay Inflation (1%)	1.980
Price Inflation (2.5%)	3.087
Corporate Risk Contingency	0.440
Landfill Tax to 31 May 2013	0.171
Highways Operations	0.600
Carbon Reduction Commitment	0.100
Employee Pension Contributions	1.300
Community Governance Review	(0.050)
Adult Services Demographic Pressures	1.000
TOTAL	**8.628**

31. The savings plans for each service grouping for the 2013/14 – 2016/17 period are summarised in the following table across the MTFP period. The table also shows the forecasted shortfall in savings which will need to be identified to achieve financial balance from 2014/15 onwards, due to the deterioration in the financial outlook as detailed above.

Service Grouping Savings Plan 2013/14 – 2016/17

Service Grouping	2013/14	2014/15	2015/16	2016/17	TOTAL
	£m	**£m**	**£m**	**£m**	**£m**
ACE	0.653	0.261	0.220	0	1.134
CAS	11.212	9.353	4.454	0	25.019
NS	4.419	2.845	1.356	0	8.620
RED	0.970	0.776	0.480	0	2.226
RES	2.137	2.510	0.564	0	5.211
Other	1.475	0	0	0	1.475
Savings to be identified	0	12.122	23.309	15.845	51.276
TOTAL	**20.866**	**27.867**	**30.383**	**15.845**	**94.961**

32. The total saving for the period 2011/12 – 2016/17 is detailed below.

Total Savings 2011/12 – 2016/17

Period	Saving
	£m
2011/12 – 2012/13	93.0
2013/14 – 2016/17	95.0
TOTAL	**188.0**

2013/14 Net Budget Requirement

33. After taking into account base budget pressures, additional investment and savings, the council's recommended Council Net Budget Requirement for 2013/14 is £457.814m. The financing of the net budget requirement is detailed below:

Financing of the 2013/14 Budget

Financing Method	Amount
	£m
Revenue Support Grant	167.162
Top Up Grant	58.223
Business Rates – Local Share	52.985
Council Tax	164.469
Council Tax Freeze Grant	2.033
New Homes Bonus	4.799
New Homes Bonus Top Slice	0.943
Education Services Grant	7.200
TOTAL	**457.814**

Capital Funding

34. The council continues to invest in capital infrastructure. An additional £3.25m of revenue will be provided in the budget to finance Prudential Borrowing to continue to support the capital programme. A key priority of the capital programme is to stimulate regeneration and job creation within the local economy.

35. The need to invest in Capital Infrastructure during the economic downturn is seen as an essential means of regenerating the local economy and for job creation. Additional investment will maintain and improve infrastructure across the County, help retain existing jobs, create new jobs and ensure the performance of key council services are maintained and improved.

36. After considering all relevant factors, the Capital Member Officer Working Group (MOWG) have recommended that additional schemes be approved for inclusion in the Capital Programme. The additional 2013/14 schemes can be afforded by utilising unapplied capital grants and utilising the 2013/14 prudential borrowing allowance not committed in MTFP for 2012/13. The new 2014/15 schemes can be afforded by utilising capital grants, capital receipts and prudential borrowing. The approval of the 2014/15 schemes will leave £10.5m of prudential borrowing still to utilise. This availability of financing in 2014/15 can be considered as part of the development the next MTFP.

37. The new investments will ensure the council continues to invest in priority projects and key maintenance programmes.

38. The 2013/14 – 2016/17 Capital Budget will be as follows:

Capital Budget

Service Grouping	2013/14	2014/15	2015/16	2016/17	TOTAL
	£m	**£m**	**£m**	**£m**	**£m**
ACE	3.959	1.260	-	-	5.219
CAS	56.046	32.005	-	-	88.051
Neighbourhoods	32.533	21.784	-	-	54.317
RED	49.318	27.379	0.725	0.027	77.449
Resources	17.605	1.645	-	-	19.250
Other	-	10.494	30.000	30.000	70.494
TOTAL	**159.461**	**94.567**	**30.725**	**30.027**	**314.780**
Financed by					
Grants and Contributions	66.498	33.661	0.271	-	100.430
Revenue and Reserves	0.987	0.807	-	-	1.794
Capital Receipts	10.000	10.000	10.000	10.000	40.000
Capital Receipts – BSF and Schools	9.774	3.000	-	-	12.774
Borrowing	72.202	47.099	20.454	20.027	159.782
TOTAL	**159.461**	**94.567**	**30.725**	**30.027**	**314.780**

39. The council has been able to set a balanced budget for 2013/14 and has a plan in place to continue to deliver local services up to 2017. Based on this, it is clear that the County Council is a going concern.

Financial Reserves

40. The County Council holds reserves:

- As a working balance to help cushion the impact of uneven cash flow and avoid unnecessary temporary borrowing – this forms part of the General Reserve.

- As a contingency to cushion the impact of unexpected events or emergencies – this also forms part of General Reserves.

- As a means of building up funds, earmarked reserves to meet known or predicted future liabilities.

41. Each earmarked reserve, with the exception of the Schools' reserve, is reviewed on an annual basis. The Schools' reserve is the responsibility of individual schools with balances at the year end which make up the total reserve.

42. A Local Authority Accounting Panel Bulletin published in November 2008 (LAAP77) makes a number of recommendations relating to the determination and the adequacy of Local Authority Reserves. The guidance contained in the Bulletin "represents good financial management and should be followed as a matter of course".

43. This bulletin highlights a range of factors, in addition to cash flow requirements that councils should consider. These include the treatment of inflation, the treatment of demand led pressures, efficiency savings, partnerships and the general financial climate, including the impact on investment income. The bulletin also refers to reserves being deployed to fund recurring expenditure and indicates that this is not a long-term option. If general reserves were to be used as part of the budget process, appropriate action would need to be factored into the MTFP to ensure that this is addressed over time so that the base budget is not reliant on a continued contribution from general reserves.

44. The setting of the level of reserves is an important decision not only for the 2013/14 budget but for the MTFP. The Quarter 3 Forecast of Outturn for 2012/13 agreed by Cabinet in March 2013 forecast an increase of £4.5m in the General Reserve Balance to £26.4m. This balance will be above the council's current reserves policy but in times of ongoing austerity, the recommended level of General Reserve should be reviewed in the light of the two new key risks identified in paragraph 26, in addition to the many associated uncertainties for local authorities in the coming years. It is therefore felt prudent for the council to consider maintaining a higher level of General Reserve in the medium term until such a time when the impact of the Business Rates Retention scheme and the Local Council Tax Support Scheme are more fully understood and Government funding reductions have ended.

45. The County Council's Reserve Policy is therefore as follows:

    (i) Set aside sufficient sums in Earmarked Reserves as is considered prudent. The Corporate Director Resources should be authorised to establish such reserves as required, to review them for both adequacy and purpose on a regular basis reporting appropriate to the Cabinet Portfolio Member for Resources and to Cabinet.

    (ii) Aim to maintain General Reserves in the medium term of up to 7.5% of the Net Budget Requirement which in cash terms equates to up to £35m.

46. Based on the level of reserves held, the County Council has demonstrated robust financial management that underpins its status as a going concern.

Risk

47. The council had previously recognised that a wide range of financial risks needed to be managed and mitigated across the medium term. The risks faced have now been exacerbated by the localisation of business rates and the localisation of council tax support. All risks will

be assessed continually throughout the MTFP period. Some of the key risks identified include:

(i) Ensure the achievement of a balanced budget and financial position across the MTFP period.

(ii) Ensure the savings are risk assessed across a range of factors e.g. impact upon customers, stakeholders, partners and staff.

(iii) The Government funding reductions are based upon Government national control total data from the December 2012 Autumn Statement. Further analysis of the content of the March 2013 Budget and the expected 2015/16 Comprehensive Spending Review in the spring of 2013 will be required to ensure estimates are updated. Recent experience would indicate that each Government financial forecast includes additional savings for local government.

(iv) The localisation of council tax support passes 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.

(v) The MTFP model builds in estimates for pay and price inflation. At the present time price inflation levels remain well above Government targets which could place significant pressure upon budgets.

48. Based on the above there are no risks which would indicate that the County Council is not a going concern.

Conclusion

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

- the body is clearly a going concern and it is appropriate for the accounts to be prepared on the going concern basis;
- 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;
- the body is not a going concern and the accounts will need to be prepared on an appropriate alternative basis.

50. Based on the assessment undertaken, in my view:

- the County Council has a history of stable finance and ready access to financial resources in the future,

- there are no significant financial, operating or other risks that would jeopardise the County Council's continuing operation.

51. Therefore the County Council is a going concern and it is appropriate for the Statement of Accounts to be prepared on that basis.

Recommendation

52. It is recommended that the County Council should be considered as a going concern and that the Statement of Accounts should be prepared on that basis.

Background papers

(a) County Council – 20 February 2013 – General Fund Medium Term Financial Plan, 2013/14 – 2016/17 and Revenue and Capital Budget 2013/14

(b) Cabinet - 13 March 2013 - Forecast of Revenue and Capital Outturn 2012/13 for General Fund and Housing Revenue Account – Period to 31 December 2012

(c) Annual Governance Report – 2011/12 – Durham County Council

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Appendix 1: Implications

Finance -

The report considers the County Council as a ‘going concern’.

Staffing -

None

Risk -

None

Equality and Diversity / Public Sector Equality Duty -

None

Accommodation -

None

Crime and Disorder -

None

Human Rights -

None

Consultation -

None

Procurement -

None

Disability Issues -

None

Legal Implications -

None