APPENDIX A

Proposed financial resilience criteria

General Comments

Finance officers at Somerset County Council have examined both the scheme and the criteria and have a number of concerns about both how such information will be used and about the content.

Clearly, in the light of Northamptonshire's continued financial position, and with statements coming from other authorities of the need to review what is the statutory level of services that they are required to provide, financial resilience is very much in the public domain. There is significant press interest as to which authority might "fail" next, and this is not helpful speculation. Somerset has suffered a great deal of interest in the trade and general press as a result, particularly after the external auditor's Value For Money report in July.

Therefore, any published index will be taken by in that light, particularly one that has been compiled by CIPFA, and is going to be used to continue this unwelcome distraction.

In terms of value to Somerset, we would have to comment that this simple RAG index would at best be of limited use. As with any competent local authority, senior leaders and finance officers at the County Council are obviously acutely aware of the financial situation that we face and are taking the necessary steps to achieve financial sustainability. Therefore, there will be limited insight that we will gain from this index.

Whilst it may be of general interest to see where Somerset sits in relation to its peers, this will not improve our financial position or mitigate the challenges that we face. Having a relative ranking of all authorities may also give a false impression, suggesting that those authorities who appear to be comparatively well off do not have any particular concerns. Given that all local authorities are facing significant financial pressures, even those who appear to be relatively more resilient may well have financial difficulties, particularly if they lie outside the services included below.

We also have some concerns about how the indices will be scored. The methodology as set out in the consultation appears to be vulnerable to a small number of "outliers", which could distort the results of all. It might be better, from a purely statistical perspective, that CIPFA considers scoring around, say, Inter-Quartile ranges.

There is also an issue around the currency of this information that is being used, compared to the latest in-year figures that will be taken to our Cabinet and Scrutiny meetings, which could cause confusion. The recent VFM report that Somerset received from our external auditor is a case in point. Whilst Somerset recognised and accepted the points that were being raised in terms of financial sustainability, it is impossible for the auditor, looking backwards, to be in the best position to acknowledge the latest work that is being undertaken to address the financial pressures. Reliance on RO returns and PSAA audit summary results, whilst published data, is similarly going to be entirely retrospective in nature.

CIFPA may wish to consider including something current, e.g. from budget monitoring reports of in-year positions, although we acknowledge that this is likely to require some resource in order to collect. However, it would be the best current position that each local authority was reporting to its members.

Response to individual indicators proposed

Indicator 1 - The level of total reserves excluding schools and public health as a proportion of net revenue expenditure.

CIPFA need to consider what they mean by “total reserves”. For example, does this include the General Reserves position, or is the intention to include earmarked reserves. Neither are entirely satisfactory. In extremis, an authority may decide to re-purpose some of its earmarked reserves in order to meet the immediate financial pressures, so if this is simply to be based on the General Reserves position, it may not show the full picture of what the authority could draw on if it needs to meet short-term expenditure.

However, if “total reserves” includes all earmarked reserves, then it could conversely overstate the funds available if some of these may not be the authority’s discretion to switch. For example, at Somerset, the earmarked reserve of the Somerset Rivers Authority (SRA) is on behalf of the SRA shadow authority, separately precepted, and could not be used to support General Reserves.

In addition, whilst there is obviously a need for a prudent level of reserves to be held in proportion to the local authority’s net revenue expenditure, this indicator would be more relevant if it also referenced the proposed usage of these reserves in future years within Medium Term Financial Plans. An authority that was not planning to use their reserves, and was able to manage a balanced budget, could be in a more resilient position than a second authority that had larger reserves but was being forced (through overspends or incomplete savings plans) to use a significant proportion of the balance each year.

Indicator 2 - The percentage change in reserves, excluding schools and public health, over the past three years.

Whilst this indicator would have some relevance as a potential danger sign, it could simply be that authorities are using earmarked reserves for the purposes that they were intended, apparently worsening the resilience. A good Somerset example is the use of significant ringfenced government grants that were received in March 2015 following the severe flooding in the County the previous winter. These artificially increased the earmarked reserves held as at 31st March 2015 and were then spent over the next 3 years. This would then have shown as a overstated reduction in earmarked reserves on this indicator.

Indicator 3 - The ratio of government grants to net revenue expenditure.

Given that RSG will be ending, we would have to question the value of this indicator.

Indicator 4 - Proportion of net revenue expenditure accounted for by children’s social care, adult social care and debt interest payments.

Whilst this indicator does have some merit, if the budget is supported by the use of reserves in one authority but not in another, then the comparison is not strictly valid. In the case of the first authority, the distorting effect of the use of reserves would actually understate the issue. This could be rectified by comparing this expenditure against the net budget adjusted for the proposed use or replenishment of reserves.

Indicator 5 - Ofsted overall rating for children's social care.

There is some overlap between this indicator and indicator 4, in that evidence shows that authorities that are rated as "inadequate" or "requires improvement" rating are likely to require additional resources over the short or medium term to make the necessary improvements. Somerset does not believe that this warrants the 15% weighting as it is effectively included above.

Indicator 6 - Auditor's VFM judgement.

It is highly probable that the external auditor will draw evidence for his or her report based on indicators 1 to 5 above. As a result, this is almost certainly double counting and we would question whether or not this indicator is actually adding to the understanding. The recent experience at Somerset would absolutely confirm that the judgement is so based. For the three year period that Somerset was rated "inadequate" for OFSTED, it was automatically deemed by our external auditor (Grant Thornton) that we would receive an "except for" opinion, regardless of any other financial or performance measures that the Council could demonstrate.

We have also noticed a level of inconsistency of approach from different audit firms in their judgements across a number of local authorities who would all seem to be facing similar difficulties, whereby some firms will make an "adverse" or "except for" opinion and other will not. Despite the NAO guidelines, this is clearly too subjective to be included.

Context

Somerset is concerned that, if this index is to happen at all, then this limited range of indicators needs to be put into a wider context, and not seen as a standalone measure of resilience. We accept that this might require more time to develop, but in our opinion, it could be more relevant if there were more indices considered (such as current budget position as stated above) and that any delay in development would be more than compensated by a more rounded picture.

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