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Dear Duncan

Somerset Council – Financial Sustainability

Following recent conversations between Grant Thornton and the Council, I am writing to express our concern over the significant financial challenges that the Council is facing and the risks that they represent to financial sustainability in the short and medium term. I would emphasise that we recognise the open and transparent engagement that both yourself and Jason Vaughan (S151 Officer) have had with us on this matter to date and also that this reflects the emerging position for the new Council five months after its formation on 1 April 2023.

Background

The Council recognises the significant financial challenges that it faces due to the impact of inflation and increases in demand and cost, particularly in relation to Adults and Childrens Services. The revenue budget forecast for 2023/24 reported to Members in September 2023 was an overspend of £26m. In addition, the medium-term financial strategy report approved in July 2023 forecast funding gaps of £42m in 2024/25 rising to £99m by 2026/27.

Recent medium term financial strategy and budget monitoring reports to Executive raise the risk that a Section 114 Notice will be required in the future. The Section 151 Officer wrote to the Department for Levelling Up, Housing and Communities on 26 September 2023 to highlight the financial challenges that the Council faces and the prospect of issuing a Section 114 Notice unless decisive actions are taken. At this time, the forecast overspend for 2023/24 had increased to £30m and the budget gap for 2024/25 increased to £80m.

Discussions with the Section 151 Officer confirm the risk that a Section 114 Notice could be required as soon as February 2024 if the current forecasts come to fruition and no corrective action is taken. We note that a range of mitigations that are currently being put in place may delay the need for such a notice until after this date.

The Council currently has a General Fund Balance of £50m and £105m of earmarked reserves. Unless the forecast overspend for 2023/24 is mitigated and actions are taken to significantly reduce the budget gap for 2024/25, there is a risk that unsustainable calls will have to be made on reserves, reducing them to levels that are insufficient to manage financial risk and fund service improvements in the future.

Initial findings

Our recent work and discussions have identified concerns over the Council's financial sustainability. The Council is in the early stages of developing plans to mitigate the financial risks it faces.

- The budget forecast reported to Members for Month 4 2023/24 was a £26m overspend caused by inflation, interest rates and the rising demand and cost of care. Adults Services are forecast to overspend by £12m and Childrens Services by £9m. The forecast overspend had increased to £30m at the time of writing to DLUHC.
- We understand that the pressures in Adults and Childrens are likely to carry forward into 2024/25. The estimated budget gap for 2024/25 is currently £80m, with a further £50m forecast for 2025/26.

- The Council currently has a General Fund Balance of £50m and Earmarked Reserves of £105m. Unless the 2023/24 overspend and 2024/25 budget gap are significantly mitigated these reserves are at risk of reducing to levels that are insufficient to manage financial risk. The prudent range for the General Fund Balance has been determined at between £30m and £50m.
- The Council has implemented recruitment and spending controls to mitigate the 2023/24 overspend.
- The Council has a strategy to reduce the budget gap in future years including a focus on 17 key budget areas, reviewing financial assumptions, and identifying service budget options.
- The Council has set up an MTFP Board, consisting of Executive Members and officers from the Executive Leadership Team to co-ordinate the budget process for 2024/25.
- Currently there is no Council-wide transformation programme or pipeline of savings to address future year budget gaps. The Council intends to bring forward the planned transformation programme to start delivering savings during 2024/25, although due to timing these savings will not be included in the 2024/25 budget.
- The Council is currently revisiting the assumptions driving the budget gap, reviewing whether earmarked reserves can be released to support financial resilience, and developing savings plans. It is anticipated that this work will be completed over the next two months in order for budget options to be presented to the December 2023 meeting of the Executive.

Our responsibilities

Under the Local Audit and accountability Act 2014 we are required to satisfy ourselves that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. When considering the Council's arrangements one of the three criteria we must report on is financial sustainability.

The Code of Audit Practice requires that where auditors identify significant weaknesses in arrangements to secure value for money, that recommendations are made setting out the actions that should be taken by the Council. The Code expects where auditors identify significant weaknesses in arrangements as part of their work, they raise them promptly with those charged with governance.

Whilst there is a risk of significant weakness in arrangements to secure financial sustainability, we recognise that the Council is fully aware of this situation and is in the early stages of implementing solutions to address the financial risks that it faces. We are also mindful that Somerset Council was formed on 1 April 2023 through local government reorganisation, and as a relatively new Council should be allowed sufficient time to develop financial plans and strategies.

Therefore, we are not raising a significant weakness or making key or statutory recommendations at this stage. We will continue to review the developing situation and the progress that the Council makes in mitigating the forecast overspend for 2023/24 and the budget gap for 2024/25. We will give continued consideration of the requirement to issue formal recommendations.

Next steps

The Council should continue its work to mitigate to 2023/24 budget overspend and bridge the budget gap for 2024/25, ensuring that reserves are maintained at prudent levels proportionate to the significant financial risks that the Council faces. Priority should be given to implementing recurring savings at pace that will benefit current and future years, and in bringing forward the transformation programme to deliver further ongoing efficiencies.

We will continue to closely monitor the Council's financial position as part of our Value for Money work for 2022/23 and consider what actions if any, we take as auditors under the Local Audit and Accountability Act 2014.

Yours sincerely

Barrie Morris

Barrie Morris, Engagement Lead
For Grant Thornton UK LLP