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Section 151 Officer current assessment of Section 114 Notice

Introduction

Section 114(3) of the Local Government Finance Act 1988 provides that "The Chief Finance Officer of a relevant authority shall make a report under this section if it appears to him [her] that the expenditure of the authority incurred (including expenditure it proposed to incur) in a financial year is likely to exceed the resources (including sums borrowed) available to meet that expenditure".

The word "shall" indicates that the actions described above are not optional, i.e. issuing a Section 114 report is something the Chief Finance Officer must do if, and as soon as, they consider that the relevant conditions have been met.

This decision should be based on the forecast level of General Fund balances at the end of the current and next financial years in line with the budget cycle.

Somerset was only able to balance its 2024/25 budget using one-off resources of £81.4m (15% of it is ongoing funding) and has a projected deficit of £103.9m in 2025/26. This is significantly more than the reserves it can apply to balance the budget.

In the Section 151 Officer Section 25 Report on the 2024/25 Budget, in respect of the Robustness of the Budget Estimates and Adequacy of Reserves it was concluded:

I have to highlight to Members my high level of concern around future years and the financial sustainability of the Council. Based upon the current forecasts there is a ***likelihood that a Section 114 notice will need to be issued in respect of 2025/26 unless there are significant changes to current forecasts.***

This report sets out the current position and risk of having to issue a s114 notice.

Section 114 Process

A report issued under s114 (3) of the Local Government Finance Act 1988 is one made by a councils Section 151 Officer known as the Chief Finance Officer (CFO) if in their opinion they believe that the expenditure to be incurred during a financial year is likely to exceed the available resources. It is considered good practice to consult the Chief

Executive and Monitoring Officer before such a report is issued. A copy of the report must be sent to all councillors and the external auditor. The Department of Levelling Up, Housing and Communities (DLUHC) must also be informed.

The report triggers a short-term statutory prohibition on entering into any new agreement which may involve the incurring of expenditure without the permission of the CFO. Statutorily the CFO can only consent to new agreements or to terminate existing agreements during this period if they will prevent the situation getting worse, improve the situation, or prevent a recurrence.

The report must be considered at a meeting of the Council within 21 days of being issued. At the meeting, the authority must decide if it agrees or disagrees with the views in the report and the actions it proposes to take.

In addition, the Government can intervene on how services are run by a council following the issuing of a s114 Report. Most councils in this situation have been the subject of such intervention via Commissioners or members of an intervention board who are usually experts with lengthy experience in local government. Ultimately, they have the power to direct a council over budgetary and other decisions.

This process has often been, mistakenly, likened to a council declaring bankruptcy. Councils legally cannot become bankrupt. In practice it is more like the process of a company entering administration in that core statutory services are maintained but the government will place commissioners in the Council to make the decisions that are needed to balance the budget, generally by cutting all non-statutory expenditure.

Context

Somerset Council is a new council formed on 01 April 2023 from the four district councils and the County Council. Despite the complexities of being a new unitary, the Council has identified the financial challenges and problems very early. This combined with the culture of openness means that the Council has been quick to highlight the concerns and take actions.

There are a range of fairly unique circumstances that have impacted upon the council and its finances. These include:-

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- **2023/24 budget** – the budget was developed through the LGR Finance Workstream. This was a very complex task due to amalgamating five separate budgets and having uncertainties around the new structure and senior leadership. As the new Council was not yet in place this involved the five predecessor councils Section 151 officers and their deputies working together.

- **Finance system** – new finance system introduced from April 2023 bringing together the financial information and systems from the five predecessor councils.

- **Staffing** – delivery of the Local Government Reorganisation (LGR) business case has resulted in the reduction of 29 senior management posts delivering £2.6m of on-going savings. However, there has been a significant loss of organisational knowledge.

- **Inflation** - peaked at a 40-year high with CPI rising to 11.1% in October 2022, although this is now starting to decrease, to 3.4% in March 2024. These inflationary increases adversely impact upon the Council and the costs of the services which it provides. This is particularly evident in the care sector where cost increases have been significantly above the CPI inflation levels. The Chancellor has announced that the national living wage will increase by 9.8% from April 2024 and the national staff pay award for 2023/24 has now been agreed at £1,925 which is estimated to be equivalent to a 6.1% increase in the pay bill for the Council.

- **Interest rate** – The Bank of England rate has risen from 0.1% in November 2021 to the current level of 5.25%. The Council is a net borrower and inherited a position of significant amount (over £200m) of short-term borrowing on 01 April 2023. Each 1% increase in interest rates has a financial impact of £2m per annum.

- **Local Government funding mechanism** – Despite the promised Fair Funding review in 2018, the updates to the systems from Government have not materialised. The system now heavily relies upon council tax as being the main element of funding for councils.

- **Council Tax** - Somerset has a historically low Council Tax. The current Band D charge at £1,646 is £381 below the English average of £2,027 for 2023/24. Council Tax was set low in 1993 against the national average and the six years of no increase at Somerset County Council and some Districts from 2010/11 has had a significant impact. The low Council Tax rate also means the Adults Social Care precept is low.

- **Adult Social Care** – there are particular issues in Somerset with increased costs due to:
    - Historically low rates paid for care home and nursing home beds.
    - Low rates no longer viable for providers following inflation, increased staffing costs, increased borrowing costs, end of Covid-19 grants which 'masked' low rates for two years.
    - More complex needs of adults following Covid-19 and lockdowns.

- **Childrens Social Care** – The medium term impact of Covid 19 and lockdowns is showing in the children's social care budget, with there being an increase in complexity of care required, resulting in greater cost.

- **Dedicated School Grant Deficit –** Following the introduction of Education Health & Care Plans (EHCPs) in 2014 and extending the age range to 24, there has been an overspend in High Need Block part of the dedicated schools grant.

- **Financial Emergency** – the council declared a 'financial emergency' in November 2023 and put in a range of arrangements to address the situation. Senior officers have formed an Emergency 'Gold' command structure to deal with the financial situation, meeting twice a week to oversee and co-ordinate activities.

2023/24 Budget Monitoring

Despite the introduction of a new finance system and not having in place a permanent staffing structure below service directors until the later part of the year, there has been monthly budget monitoring reports starting in month two with an 'emerging issues' paper. The budget monitoring reports are formally reported to both Scrutiny and Executive on a monthly basis. The format of the report has been refined and continues to evolve to highlight the key issues and actions.

There have been some actions taken during the year to address the potential in-year overspend and these include:

- **Directorate level financial controls** that were agreed by the Executive as part of the month three budget monitoring report and cover:

- Delivery of 2023/24 savings
- Staffing establishment controls
- Underspending opportunities from 2022/23
- Transaction limits
- Local schemes of delegation
- Non-critical spend
- Value engineering
- Exploring alternative funding mechanisms

- **No PO, No Pay** – on the back of the introduction of the new finance system, tackling and working with services on ensuring the follow good financial management practice and issue Purchase Order when committing funds.

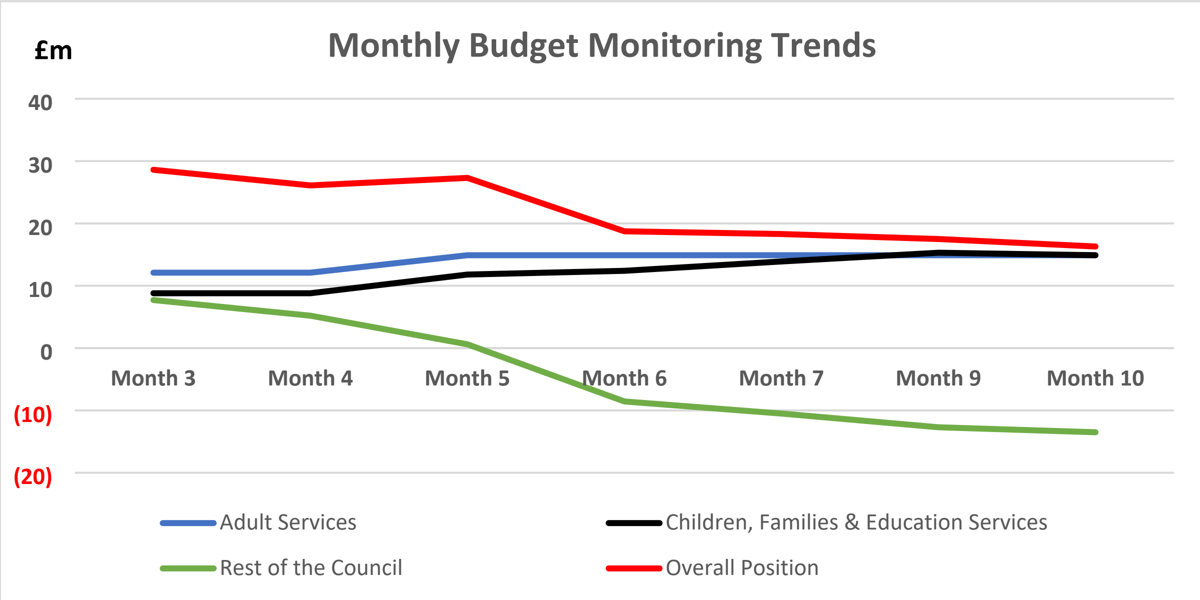
- **Financial training** – there has been a significant investment in the training of staff on the new finance system to enable them to use and understand the new processes which assists with more accurate budget monitoring processes.

- **Control Boards** - the directorate level financial controls were not having the desired impact and needed strengthening. Due to this a number of daily and weekly control boards have been put in place: -
  - Establishment & Recruitment Control Board - to assess all workforce requests and changes.
  - Commercial & Procurement Control Board – to review and challenge all new commissions, annual uplifts in contract and contract renewals.
  - Spend Control Board – ensuring that all purchases over £100 are reviewed and challenged to avoid any non-essential spend.
  - Adult Social Care Panel – to review and challenge placements.
  - Childrens Care Panels – various panels to review and challenge placements.

- **Staff messaging** – the intranet, staff and management briefings have all been utilised to publicise the council's financial position and the need to reduce down the in year overspend.

The impact of the various interventions has resulted in the forecast overspend being reduced £12.3m, from £28.6m to £16.3m.

However, the overall picture masks the underlying issue of both Adults and Childrens deteriorating positions, with the month three budget monitoring report showing their combined forecast overspend of £20.9m increasing to £29.8m by month ten. The rest of the Council has seen a dramatic reduction of £20.4m over the four months from a forecast overspend of £7.7m in month three to a forecast underspend of £12.7m in month ten.



2024/25 Budget

The Financial Strategy was approved by the Executive in July 2023 and updated in the light of the 'Financial Emergency'. It has been focused upon avoiding a section 114 notice by taking the actions that a Commissioner would take. The actions and progress are summarised below:

Financial Strategy Area	Progress & Actions
Reducing the current year's overspend	Overall overspend reduced from £28.6m to £16.3m. This reduces the call on General Reserves by £12.3m. General Reserves would be reduced down to £33.6m (£49.8m - £16.3m) and means they would exceed the minimum level of £30m.
Reviewing and reducing budget pressures	Every Service subject to a Service Challenge Session review by peer group using the financial strategy key line of enquiry. there were also 'Deep dive' sessions for Adults (involving LGA national expert + Newton) and Children & families (involving Peopletoo).

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Financial Strategy Area	Progress & Actions
	Impact has been reduction of £3.8m from the November 2023 forecast
Identifying further saving options	Every Service subject to a Service Challenge Session review by peer group using the financial strategy key line of enquiry. there were also 'Deep dive' sessions for Adults (involving LGA national expert + Newton) and Children & families (involving Peopletoo). Impact has been identification of £24m of new savings for 2024/25 bring the total savings up to £35m, with a further £10.5m identified for the following year.
Reducing the capital programme and bids for new schemes	The initial bids for new capital totalled £227.0m, with a new borrowing requirement of £116.6m. These have been reviewed and reduced down to £112.7m with borrowing requirement of £3.3m. The overall capital programme for 2024/25 to 2026/27 totals £238.5m with a borrowing requirement of £44.4m with the revenue effects being built into the MTFP.
Maximising funding & income to the council	These have been included with the savings proposals with fees & charges & other income totalling £6.8m
Generating capital receipts from asset disposals	Asset Management Group receive regular updates on progress. £4.7m disposals achieved in the current financial year with potential to increase to £7.7m. Profile of disposal over next three years completed with 2024/25 of £8.5m and additional high risk of £5.6m, 2025/26 of £8m with high risk

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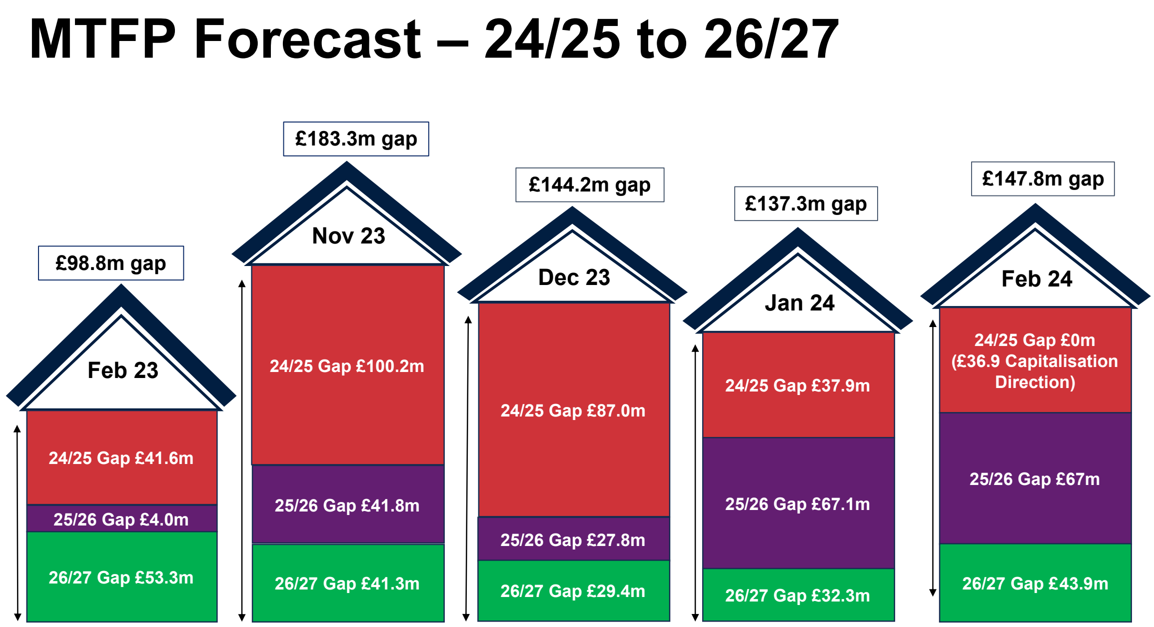
Financial Strategy Area	Progress & Actions
	of further £7.3m and 26/27 of £8m high risk. Total potential of £45.1m.
Disposing of commercial investments	JLL engaged to review portfolio and initial finding have highlighted phasing of £69.6m in 2024/25, £86.8m in 2025/26 and £38.3m in 2026/27. Resulting in loss of income from disposal of £6.3m, £8m and £4.1m.
Completing the outstanding statement of accounts from the processor councils,	There were a number of outstanding statements which could adversely impact upon Somerset Council and represent a significant risk. Good progress has been made and now the outstanding ones have been completed:- 2020/21 – Sedgemoor 2021/22 – Mendip, Sedgemoor, South Somerset – complete 2022/23 – Mendip, SWT, Somerset CC & Pension Fund – all complete The only outstanding accounts related to 2022/23 for South Somerset & Sedgemoor which are expected to be completed by March 24 ahead of the cut off period.
Reviewing Earmarked Reserves and repurposing them to support the budget,	Repurposing of several reserves from the predecessor councils to boost general reserves to £9.8m to cover the current years potential overspend and £36.8m identified put into a MTFP Support Reserve to support the 2024/25 budget.
'Resizing' of the organisation (workforce transformation) to enable it to become financially sustainable in the future	Outline business case needs to be produced for February 2024 Executive to give authority to commence process. Without a clear plan there is a significant risk that the implementation costs cannot be afforded. The business case needs to demonstrate a clear payback period and avoid the

Financial Strategy Area	Progress & Actions
	mistakes of other councils of removing posts with no clear plan on services will operate and then having to reinstatement at significant cost.
Working with DLUHC on a capitalisation direction.	The Minister for Local government has written to the Council with a “minded to” approval for a capitalisation direction of £76.9m for 2024/25. Final confirmation is expected towards the end of March.

The chart below shows the progress in reducing the budget gap for 2024/25 from the £100.2m reported to the Executive in November 2023 down to £36.9m prior to any Capitalisation Direction from DLUHC. It also shows how the overall MTFP Gap has reduced by from £183.3m to £147.8m.



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The table below shows the detailed breakdown across the services. It shows that the 2024/25 budget proposals addresses the overspend in both Adults and Childrens in the current year. The proposals also include maintaining £6m in corporate contingency and an allowance for the national pay award.

Service Area	2023/24 Budget £m	2024/25 Budget £m	Change £m
Adult & Health Services	181.3	239.4	58.0
Children & Family Services	126.1	142.0	15.9
Community Services	37.0	35.5	(1.5)
Climate & Place	94.2	93.9	(0.3)
Strategy, Workforce & Localities	25.5	24.7	(0.7)
Resources & Corporate Services	23.3	27.7	4.4
Public Health	1.0	1.0	0.0
Corporate Areas:			
Pay award	-	10.3	10.3
Debt financing	40.7	53.6	12.9
Other Corporate costs	13.7	10.6	(3.1)
Capitalisation Direction	-	(36.9)	(36.9)
Net Budget Requirement	**542.8**	**601.8**	**59.0**
Financed by:			
Council Tax	(335.5)	(357.8)	(22.2)
Flexible Use of Capital Receipts	(4.0)	0.0	4.0
New Homes Bonus	(3.8)	(1.9)	1.9
Rural Services Delivery Grant	(3.2)	(4.1)	(0.9)
Services Grant	(3.2)	(0.5)	2.7
Social Care Support Grant	(39.2)	(51.0)	(11.8)
Revenue Support Grant	(7.9)	(8.5)	(0.5)
Business Rates	(122.2)	(128.4)	(6.3)
Council Tax Somerset Rivers Authority	(3.0)	(3.1)	0.0
Special Expenses	(0.2)	(0.2)	0.0
Business Rates Collection (Surplus) / Deficit	6.1	(1.5)	(7.6)
Council Tax Collection (Surplus)	(6.7)	(6.2)	0.4
General Reserves	-	-	-
Earmarked Reserves	(19.9)	(38.5)	(18.6)
Total Financing	**(542.8)**	**(601.8)**	**(59.0)**

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The table below summarises the changes from the 2023/24 budget for both costs and funding. Out of the total Pressures of £108.5m, Adults of £69.6 and Childrens of £26.4m, make up 88% of the change to address the current years overspend and forecast increases for 2024/25. The savings of £35.2m represent over 6% of the total budget with Adults and Childrens making up £19.3m (55%) of them.

There are £81.4m of one-off items which enable the budget gap to be closed. This obviously creates a corresponding pressure in 2025/26.

Changes to 2023/24 budget	**£m**
Reversals for once off items	19.9
Pressures	109.9
Savings	(35.0)
Changes to pay	13.8
Increase in financing costs	12.9
Increase in funding	(40.1)
Budget gap	**81.4**
One off items – to balance budget	
Use of Medium-Term Financial Plan Support Reserve	(36.8)
Council Tax Collection Fund surplus	(6.2)
Business Rates Collection Fund surplus	(1.5)
Capitalisation Direction	(36.9)
Remaining budget gap	**0.0**

Reserves

The new Council had a comparatively reasonable level of reserves on vesting day, 01 April 2023. £20m of reserves were planned to be used in 2023/24 with £10m of these used to balance the budget. Early in the new financial year it became apparent that more reserves would be required to fund the forecast overspend in 2023/24 and to support the 2024/25 budgets. A detailed review of the inherited reserves to determine if any could be released to support both financial years was undertaken in November 2023 and the re-classification reported to Executive on 06 December 2023.

The review of the reserves resulted in:

- A transfer between the Earmarked Reserves to General Reserves to increase them to £49.8m
- Repurposing of several reserves from the predecessor councils to create a MTFP Support Reserve of £36.8m which is planned to support the 2024/25 budget.

The level of General Reserves will be reduced from £49.8m by the Month 10 forecast overspend of £16.3m to give £33.5m. This is above the current risk based minimum level of £30m. There is therefore no immediate risk of running out of reserves in the current financial year.

DLUHC

At the Full Council meeting on 20 December 2023, the Council resolved to formally request a capitalisation direction from DLUHC in order to set the 2024/25 budget and avoid a Section 114 Notice.

An application is for an additional 5% increase in council tax for 2024/25 was turned down by DLUHC and obviously has an adverse impact upon future financial sustainability given that it would have generated £17.1m of on-going funding whereas the capitalisation direction and use of reserves are one off.

To create a financially sustainable council, proposals for a significant reduction in the workforce are planned which will deliver on-going savings of £20m to £30m for 2025/26 (in addition to those in the LGR Business Case). The one-off costs of this are estimated to be in the region of £40m. Further work is being undertaken to assess if some of these costs can be funded from the flexible use of capital receipts.

The total request for 2024/25 is £76.9m, with £36.9m to balance the budget and £40m for the implantation costs of the planned reduction in workforce.

Annual Audit Report

Grant Thornton has produced their Annual Audit Report which was presented to the Audit Committee on 25 January 2024 and full Council on 20 February 2024.

In completing this assessment, Grant Thornton have looked at the arrangements in place for the continuing authority Somerset County Council and three of the legacy District Council's (South Somerset District Council, Somerset West and Taunton

District Council, and Sedgemoor District Council) for the 2022/23 financial year. Grant Thornton were not the appointed auditor for Mendip District Council for 2022/23. EY will be producing the Annual Audit Report for Mendip DC.

Grant Thornton have made no statutory recommendations to the Council as a result of their findings, but they have made seven key recommendations and six improvement recommendations.

Risks, Assurance, External Validation & Reviews

A common feature of councils that have issued a section 114 notice has been the number of prior year external audits that have not been completed. Therefore, a key area of activity for the finance team in the new Council has been around the production of the 2022/23 statement of accounts for the five predecessor councils and dealing with the inherited position of outstanding external audits on their accounts from 2020/21 and 2021/22. This is particularly important, not only in understanding the opening position for the new Council, but also in providing independent external assurance around the finances. Good progress has been made on this, with all the 2020/21 and 2021/22 statement of accounts now signed off. All five of the 2022/23 statements of accounts have been published and three of these have been signed off by the external auditors, with the remainer being completed in March 2024.

There have been regular Member briefings on the Council's finances which started in August 2023 and there have been two monthly briefing sessions open to all members from September 2023 and these will continue through to February 2024 to ensure that all members are aware of the financial challenges that the Council faces.

There have been a number of external reviews which have been carried out to help validate the overall budget and potential savings, some leading to change programmes. These include:

- Adult Services commissioned Newton Europe to complete a transformation programme "My Life, My Future" following a diagnostic review in 2022. The programme is aimed at improving outcomes for older adults, those with learning disabilities and mental health needs by helping them stay within their own homes and encouraging independent community support. The programme is aimed at reducing costs by circa £14m per annum on an ongoing basis by reducing the number of residential placements.

- Children's Services have commissioned Peopletoo to undertake a review of spend in Children's Social Care to determine a plan for better outcomes at a reduced cost from using best practice.

- PDLB Financial Consultancy Ltd was commissioned to undertake an independent review of the new Council's balance sheet. Comparing it to statistical neighbours and highlighting whether particular issues need to be built into the 2024/25 budget or changes in practice made. This fulfils part of the recommendation in the report to the July 2023 Executive to undertake a financial resilience review. The report will be presented to the Audit Committee on 25 January 2024 with their recommendations passed to the Executive meeting in February 2024.

- Peopletoo have been commissioned to undertake a review of third party spend, this work will highlight opportunities for ongoing savings and will be implemented later in the financial year.

- Peopletoo were commissioned have reviewed the processes for collecting client contributions for elements of Adult Care services to determine that all income is being recovered. As a result of this review £3.4m of additional income has been identified and included as part of the budget proposals.

Areas of concern

There are a number of areas where I have concerns and it is worth highlighting these as they may impact on future S151 assessments. The areas of concern are:-

- **DLUHC** –Discussions with DLUHC have been positive and they understand our financial position and circumstances, but did not approve the request for the additional 5% on council tax. This has an impact on the councils medium term financial sustainability. Their process for approving capitalisation directions does not fit the legal timetable for councils' budget setting. Their 'minded to' letters have no legal standing and therefore can't be relied upon. This could be an issue for setting the 2025/26 budget and could force a section 114 notice if there is insufficient savings or reserves available to set a legally balanced budget.

- **Dedicated Schools Grant (DSG)** – the table below summarises the latest projected increase in the DSG deficit. Although there is currently a statutory override, this is due to end on 31 March 2026. At this stage the deficit would be set against the council reserves and based upon the latest forecast would likely trigger a section 114 notice unless there are significant changes, or the statutory override is extended.

DSG deficits	31/03/2023 Actual £m	31/03/2024 Forecast £m	31/03/2025 Projected £m	31/03/2026 Projected £m
DSG deficit	20.7	37.5	56.5	72.2

- **2023/24 Budget Outturn** – there has been an overall positive downward trend, but I remain concerned about both Adults and Childrens. Childrens are a particular concern giving that the overspend forecast in month three was £8.8m and has increased to £14.9m in month ten.

- **Disposal of Assets** – the overall financial strategy for 2024/25 is based upon the disposal of both commercial and non-commercial assets. Given the nature of property transactions, members views and the external market this remains an area of concern that will need to be carefully monitored.

- **Level of Reserves** – although General Reserves are currently £49.8m they will be reduced down by the 2023/24 overspend. On the latest forecast they will remain above the minimum agreed level of £30m but not significantly. The amalgamation of reserves and repurposing of £36.8m to support the budget means that there is little flexibility in the remaining reserves to cover any unforeseen circumstances.

- **Delivery of Savings** – the experience in the first year of the new council has been that a number of savings built into the budget have not been delivered. Given that a further £35m of savings have been built into the 2024/25 budget this can not happen given the adverse impact this would have on reserves.

- **New Savings** - the budget gap for 2025/26 is currently forecast as being £103.9m and will require a significant level of new savings. These need to be both identified and then delivered. Given that reductions in staffing will be a substantial part of these, careful monitoring of their deliver will be required.

- **Improvement and Transformation Programme** – the work on having a comprehensive organisational wide transformation programme is still embryonic. The timelines, detailed business cases around the workforce are critical given its financial impact.

- **Delivery of the Workforce Transformation** – the safe delivery of the estimated £30m to £40m savings from reductions is a vital element of the council achieving financial sustainability. There is experience of other councils undertaking similar large scale programme and these do present significant risks around service delivery and implementation costs which will need to be actively managed.

Summary & Conclusion

The 2023/24 in-year forecast overspend has continued to be reduced as the mitigations and additional financial controls put in place continue to have a positive impact. The Council has just set the 2024/25 budget, with £81.4m of one-off resources were required to close the budget gap. The current MTFP forecast has identified that budget gap for 2025/26 of £103.9m.

Despite the 2024/25 financial year not having commenced, work is already progressing on delivering a balanced budget for 2025/26, ideally without the need for a further capitalisation request.

High level savings targets have been assessed with responsible officers identified to lead the work with a current range of potential savings of between £47m and £116m.

The issuing of a s114 notice will therefore be dependent on three major areas that will be monitored through the year:

- The Council delivering the savings agreed in setting the 2024/25 budget and containing pressures within the growth allocated.
- Progress on preparing detailed, deliverable business cases for 2025/26 over the next six months in line with the high-level targets set out in appendix 3.
- The local government financial settlement for 2025/26 and future flexibility on Council Tax increases.

Taking into account all of the above, **there is no need to issue a Section 114 Notice** at this stage. The situation will be kept under close review.

Jason Vaughan FCCA, CPFA, IRRV (Hons)
Executive Director – Resources & Corporate Services (Section 151 Officer)