



Letter to Members of Northamptonshire County Council

EXECUTIVE DIRECTOR OF FINANCE

Subject:	Report under Section 114 of the Local Government Finance Act, 1988
Recommendations:	That Members of the County Council note this report and the actions taken by the s151 Officer. That the report is discussed at the meeting of the County Council on 22 nd February 2018.

1. Purpose of report

- 1.1 Members of the County Council are asked to consider this report by the Section 151 Officer (s151, Chief Finance Officer).
- 1.2 The Local Government Finance Act, 1988 places certain responsibilities on the Chief Finance Officer, namely (para 3): *“The chief finance officer of a relevant authority shall make a report under this section if it appears to him that the expenditure of the authority incurred (including expenditure it proposes to incur) in a financial year is likely to exceed the resources (including sums borrowed) available to it to meet that expenditure.”*

2. Background

- 2.1 The County Council has faced a serious financial problem for some years. This situation has attracted professional, political and press attention over a sustained period. The County Council is currently subject to a Best Value Inspection at the behest of the Secretary of State for Housing, Communities and Local Government.
- 2.2 At the time of writing the County Council faces an overspend of £21.1 million for the financial year 2017/18. This position has been arrived at by the recent failure to sell the asset known as Buckton Fields. This was budgeted to generate a capital receipt of £12 million which was intended to be used to finance revenue spending on Transformation. The County Council has available reserves of £12 million. Thus, as things stand, and as on the current available information, the County Council would be in danger of ending the financial year 2017/18 with a negative General Fund balance unless action is taken. This would represent a breach of the relevant legislation. Although this Section 114 notice is concerned with the immediate position I am also conscious of the gaps identified in the Medium Term Financial Plan.

- 2.3 At the Cabinet Meeting of 13th February 2018 Members will be asked to agree to the sale and leaseback of One Angel Square as a mechanism to generate a capital receipt that can be used according to HM Government's flexibility in the use of such receipts to pay for revenue spending, as long as that spending is on qualifying Transformation activities (where in this context transformation means investment in services in order for those services to be able to operate in new and more efficient ways). This is a legitimate option to deal with the pressures in the current year and has been developed by senior officers, but it has had to be developed quickly given the proximity of the end of the financial year.
- 2.4 The sale of One Angel Square under the proposed sale and leaseback continues to be my recommendation as the Council's s151 officer. However the sale and the application of the receipt contain sufficient risk for the outcome, and the thus the end of year financial position to be subject to uncertainty. This risk is in the following categories:
- Timing risk – that it proves not to be possible to complete the exchange of contracts in time to include the receipt in the Council's outturn for 2017/18;
 - Market risk – that it proves not to be possible to attract a viable bid from an acceptable counterparty;
 - Regulatory risk – that it proves not to be possible to agree an acceptable accounting treatment, or that the application of the receipt to a sufficient quantum of qualifying transformation expenditure is not achievable.
- 2.5 In these, or other possible circumstances the County Council will reach the end of the financial year 2017/18 with no ability to take action to seek to mitigate the situation.
- 2.6 At the same time the County Council operates in an environment where the risk of unexpected spending pressure cannot be ruled out. I have not been in post as the Council's Chief Finance Officer long enough to obtain complete assurance to the scale of this risk, the extent of hidden risk, or the efficacy of the control environment to mitigate the risk.
- 2.7 I also have concerns about the application by the County Council of the flexible use of capital receipts in the current year and whether the full amount that is currently allocated to this can be justified. I will not be able to form a judgement on this until after further investigation.
- 2.8 For these reasons it is imperative, in my professional opinion and as the Council's s151 officer that the County Council takes steps to mitigate this serious financial risk so that if any of the risks described above came to pass the County Council stood as strong a chance as possible of avoiding an unfunded overspend. If the risks were in fact able to be mitigated then the action taken as a consequence of the Section 114 report would serve to increase the County Council's financial resilience to meet future challenges.
- 2.9 The purpose of this Section 114 notice is to make it clear to Members of the County Council that it faces a financial situation, in the current year and for

2018/19 of a serious nature. This is a situation that cannot simply be left for officers to improvise solutions. The Members of the Council must take responsibility.

- 2.10 A Section 114 requires the Chief Finance Officer, in consultation with the Council's Monitoring Officer, to report to all the authority's members if there is, or is likely to be, an unbalanced budget set. This includes situations where reserves have become seriously depleted and it is forecast that the Council will not have the resources to meet its expenditure in a particular financial year.
- 2.11 This Section 114 notice has serious operational implications. The full Council must meet within 21 days to consider this notice. The scheduled Council meeting of 22nd February 2018 represents the ideal opportunity. During the period between now and the 22nd February 2018 the Council is prohibited from entering into new agreements involving spending.
- 2.12 In practice this means that all *new* spending is prohibited between now and the 22nd February 2018. The County Council has serious responsibilities, not least in connection with its statutory responsibilities towards Children and vulnerable adults. Therefore I will introduce a mechanism that allows proposals for urgent spending to be considered and, if appropriate, approved. This is likely to take the form of a weekly, or more frequent, spending approval panel chaired by the Interim Chief Executive. All other new expenditure will be stopped. This includes, *inter alia*, works against contracts, the hire of new permanent or temporary staff, and all avoidable spend on IT and other assets and consumables. The use of GPC cards will not be allowed, except in emergency circumstance
- 2.13 The Council must proceed with setting its budget for 2018/19. It is essential that the precept is issued so that the Boroughs and Districts can collect the Council Tax income due to the County Council. There can be no change to the precept once set and if changes to budget plans are required during 2018/19 they will be changes to expenditure plans or through income generation. The ability to have a balanced budget for 2018/19 is also dependent on the proposed sale and leaseback of One Angel Square. However there is also risk that the quantum of qualifying transformational expenditure does not match the capital receipts that can be applied. In either circumstance cuts to expenditure would have to be undertaken during the 2018/19 financial year and I will have to form a judgement on whether to continue with or modify the spending controls outlined above.
- 2.14 The introduction to the Section 25 report appended to the 2019/19 Budget report (as slightly updated), which is reproduced below, is my assessment of the sustainability of the Budget and Medium Term Financial Plans. This assessment is useful background to this Section 114 notice and contains a description of the gravity of the financial situation facing the County Council.

Mark McLaughlin, BSc (Hons, St A), PhD, CPFA

Report of the Chief Financial Officer on the robustness of the budget estimates and the adequacy of the reserves (*Extract*)

Section 25 of the Local Government Act 2003 places a duty on the chief finance officer (the strategic director and chief finance officer) to make a report to the council on the robustness of the estimates and the adequacy of the reserves. This report fulfils this requirement and provides councillors with assurance that the budgets have been compiled appropriately and that the level of reserves is adequate. It is a statutory requirement that councillors must consider this report when considering and approving a budget.

In presenting this report the chief finance officer is mindful of other associated statutory safeguards designed to prevent the authority from over-committing itself financially:

- Section 151 of the Local Government Act 1972 which requires the authority to make arrangements for the proper administration of its financial affairs and that the chief financial officer has personal responsibility for such administration;
- Sections 32, 43 & 93 of the Local Government Finance Act 1992 which requires the authority to set a balanced budget;
- The Prudential Code introduced as part of the Local Government Act 2003 sets out the framework within which the authority must manage its investments, including adequate planning and budget estimates;
- The external auditor's duty to assess the adequacy of the authority's proper arrangements to secure economy, efficiency and effectiveness ('value for money').

To reinforce these obligations, section 114 of the Local Government Finance Act 1988 requires the chief finance officer to report to all the authority's councillors, in consultation with the Monitoring Officer, if there is or is likely to be unlawful expenditure or an unbalanced budget.

Introduction

In considering the setting of the County Council budget for 2018/19 two key facts must be recorded and absorbed:

The Council entered the 2017/18 financial year with a budget that proved inadequate in the face of the pressures experienced. The 2017/18 budget introduced more challenge, but elements of the structural deficit take time to eliminate. This has meant an overspend in 2017/18 which has an influence on the 2018/19 budget. It also demonstrates the importance of complete realism in budget setting. The paucity of reserves means that the accuracy of the budget and the delivery of savings and avoidance of overspending during 2018/19 is essential.

The County Council faces an unprecedented set of challenges in setting the 2018/19 budget.

In common with all county councils, Northamptonshire has had to deal with the consequences of a local government finance system that does not properly recognise the impact of demographics and demand. However past decisions on spending and income, including the

level of Council Tax set, have contributed to the County Council having very little room for manoeuvre in setting its budget for 2018/19.

Members of the County Council should be in no doubt that the Council faces a financial situation that is grave and which thus places strict limits on the choices available to the County Council.

Prior to 2011 a local authority in the circumstances facing the County Council would have been best advised to address its financial sustainability via an appropriate increase in the level of Council Tax. In the current legislative environment a proposed Council Tax increase exceeding 5.98% would have to be put to local voters using a referendum. In practice this is a hurdle that may be impossible to conquer and so the proposed level of increase in Council Tax is limited to 5.98%. Although this exceeds the current level of inflation the increase in demand, means that while it is a contribution to financial sustainability it is far from sufficient.

Council Members will be aware that the extra 1% increase in Council Tax allowed by HM Government since the draft budget was written has attracted attention along the lines of how the unexpected "extra" money will be spent. Council Members have to be clear that while this 1%, if approved, will add £2.7 million to the County Council's income compared to the draft budget, the *further* pressures identified since the draft budget amount to £18.1 million. This is a sum that exceeds the £2.7 million by a factor of 7. Thus there is no unexpected extra money to be spent but in fact a minor contribution to a financial position that is unprecedented in its gravity. While speculation on the use of the £2.7 million is unavoidable in the press and on social media, Council Members have had access to advice from qualified and experienced local government finance professionals and have thus being able to avoid similar speculation.

The budget-setting process has included a new rigour including detailed Cabinet Member involvement through the Star Chamber process. Chief Officers have risk-assessed all of the proposals included in the draft budget and advised the removal of those which are not deliverable. This added £3.7 million to the pressures facing the County Council.

New pressures have become clear since the draft budget was set, including a likely £6 million cost of sleep-in allowances. These costs have to be accounted for in the pressures noted above of £18.1 million (and in the case of the sleep-in allowances will be included as an earmarked reserve, to be released only to meet sleep-in costs when the Executive Director of Finance is satisfied in relation to discussion with individual providers).

The 2018/19 budget also features, for decision, the cost of the additional 1% pay increase, as per the national offer and beyond the 1% in the draft budget. This recognises the real risks of recruitment and retention faced by the County Council.

The budget for 2018/19 is heavily influenced by the project financial outturn for 2017/18.

The County Council entered 2017/18 with minimal reserves, and a budget that was achievable only with ambitious savings proposals and via inherently risky asset sales. In the event the County Council faces an overspend of £21.1 million for 2017/18, of which around half is the consequence of delayed capital receipts.

The County Council only has reserves that would meet half of this overspend. This is why the sale and leaseback of One Angle Square is being expedited in the current year. Council Members need to be aware that the alternative would be to close the year with a negative General Fund balance. This would be an unprecedented prospect and, if at all likely, would lead to formal action by me in my role as the s151 Officer via an s114 report. This may still be necessary should the projected sale and leaseback not prove possible or if other spending

risk becomes apparent. In such circumstances rapid and difficult reductions in non-statutory services would be unavoidable.

The potential sale proceeds from One Angle Square is also required in order to set a balanced budget for 2018/19 through carrying forward around £20 million of the receipt to pay for qualifying expenditure in 2018/19. Doing so takes advantage of the continued Capital Receipts Flexibility announced as part of the Local Government Finance Settlement in December 2017.

However Council Members have to be clear that the use of one-off monies to support ongoing expenditure can never be a sustainable financial strategy. The use of asset sales to generate receipts can only be a stop-gap until financial sustainability can be gained.

Council Members must also be very conscious of the fact that only qualifying expenditure on Transformation can be met from these capital receipts. Should the quantum of qualifying transformation activity that can be charged to the flexible use of capital receipts be less than the overall revenue gap then that gap will have to be filled through the elimination in whole or in part of expenditure on non-statutory functions. This analysis will be closely monitored during 2018/19. However it is more likely to become a significant factor in setting the budget for 2019/20 and beyond. In simple terms it may not be possible to close the budget gap through applying capital receipts as the size of the gap may exceed the amount of qualifying expenditure. The only recourse at that point will be the elimination of non-statutory spending and this would almost certainly involve, again, a further set of difficult decisions.

The County Council's ability to set balanced budgets beyond 2018/19 will be dependent on further asset sales, but can only be in any way sustainable through 2019/20 and 2020/21 through cost reduction, demand control, rigorous financial control and iron discipline in decision making and delivery. Income generation will need to be maximised, through attention to fees and charges. The investment in the Transformation of the Council's services is aimed at the control of costs in the face of demand. Financial control has been improved during 2017/18 but will require further attention and rigour and I have accepted this is a personal priority. However the demonstration of financial discipline is something that must be led by decision makers – i.e. the members of the County Council and in the current circumstances this should begin with the acceptance of the maximum number of realistic savings options, including those which have proved controversial or unpopular during the consultation process since the draft budget. Reversing the consulted-upon savings options on Libraries, Bus Subsidies and Trading Standards to the value of £1.56 million – as proposed in this budget – may not be sustainable even in the short term.

The long term financial sustainability of the County Council cannot be delegated to external agents. HM Government have promised that a new system of local government finance will be introduced for 2020/21. However HM Government's fiscal plans do not hold out much prospect of a significant increase in the resources allocated to local government. A new finance system is more likely to be concerned with the distribution of an ever-shrinking quantum of support rather than a major injection of spending power. Sustainability for local government in Northamptonshire is more likely to be helped by reorganisation leading to the creation of one or more unitary authorities in the County with explicit cost saving through reduced costs of business. Achieving this will require leadership, partnership and a focus on the needs of the residents of the County and suppression of the vested producer interests, including those of local government members and officers.

Even so the fundamental contribution to the financial sustainability of the County Council has to come from decisions made by Council Members and the starting point must be a realistic and sustainable budget for 2017/18.