Agenda Item No: **17**

Wolverhampton City Council

Audit Committee

22 September 2014

Report title	Independent review of process for medium term financial strategy and budget
Cabinet member with lead responsibility	Councillor Andrew Johnson Resources
Accountable director	Keith Ireland, Delivery
Originating service	Audit
Accountable employee(s)	Mark Taylor — Assistant Director Finance Tel — 01902 556609 Email — Mark.taylor@wolverhampton.gov.uk
Report to be/has been considered by	Strategic Executive Board — 17 July 2014 Confident Capable Council Scrutiny Panel — 10 September 2014

Recommendation(s) for action or decision:

The Committee is recommended to:

1. Review and comment upon the recommendations from the independent review and the action plan developed to address those recommendations.

1.0 Purpose

1.1 To review and follow up the recommendations from the Independent Review of Process for the Medium Term Financial Strategy and Budget.

2.0 Background

2.1 During the 2013/14 budget process there was concern regarding the large deficit that was projected and therefore SEB agreed to commission an independent review of the financial planning and budgeting process.

2.2 The Local Government Association (LGA) recommended a suitably qualified independent reviewer, Eugene Sullivan ex chief executive of the Audit Commission. Eugene Sullivan was engaged for the review and produced his final report on May 2014.

2.3 The final report is attached as Appendix 1.

3.0 Independent Review Report

3.1 The review was conducted using a combination of personal interviews with lead Councillors and officers, plus External and Internal Audit together with a review of the appropriate papers and spreadsheets.

3.2 The results of the review were positive concluding that the approach to five year planning is as good as those seen anywhere else. There is a thorough approach to identifying assumptions and making reasonable (not optimistic or pessimistic) assumptions for the next five years. The financial reports which go to Cabinet are well constructed, well drafted and make good use of narrative, tables and graphics.

3.3 The review made 7 relatively minor recommendations for improvement. These included producing shortened and simplified reports (which has already been implemented) in order to communicate the message more effectively to Councillors and other stakeholders.

3.4 It is recommended that all the recommendations from the review be adopted and that the Action Plan included at Appendix 2 is implemented in order to address those recommendations over the course of next budget cycle.

3.5 The review was commissioned by SEB to provide assurance to officers that the Council's financial planning and budgeting processes are robust. The results of the review are now being communicated to Councillors in order to provide further assurance in this area.

4.0 Financial implications

4.1 There are no direct financial implications arising from this report although the independent review confirms that the Council's financial planning and budgeting processes are robust and implementing the recommendations will further improve financial control.

[NA/10092014/R]

5.0 Legal implications

5.1 There are no direct legal implications arising from the report.
[AS/16092014/Q]

6.0 Equalities implications

6.1 There are no direct equalities implications arising from the report.

7.0 Environmental implications

7.1 There are no direct environmental implications arising from the report.

8.0 Human resources implications

8.1 There are no direct human resources implications arising from the report.

9.0 Corporate landlord implications

9.1 There are no direct corporate landlord implications arising from the report.

10.0 Schedule of background papers

10.1 None.

Appendix 1

WOLVERHAMPTON CITY COUNCIL

INDEPENDENT REVIEW OF PROCESS FOR MEDIUM TERM FINANCIAL STRATEGY AND BUDGET

PREPARED BY
EUGENE SULLIVAN, CPFA (HONS)
30 May 2014 (Amended 11 July 2014)

INTRODUCTION AND CONTEXT

Wolverhampton City Council (WCC), in common with many local authorities and other publicly funded bodies, faces a significant financial challenge caused by the coincidence of reduced sources of funds and increased demand for services, particularly in relation to care of Adults and Looked after Children. In line with good practice WCC maintains a sophisticated financial model to help manage its financial strategy over the medium term (5 years). This model is a dynamic living model which is updated regularly for new circumstances and assumptions. The WCC Cabinet met on 25 February to consider the 5 Year Budget and Medium Term Financial Strategy (MTFS) based on the up to date projections.

The MTFS forecast five year expenditure plans and the resources available to fund those plans. The MTFS showed that expenditure plans exceeded resources by just over £123 million. The MTFS included savings proposals close to £65.0 million. Assuming these proposals are fully achieved, as profiled, the Council needs to identify and achieve further savings of just over £59 million over the five year period.

The scale of the challenge prompted the Council to commission an independent public sector finance professional to conduct a short review and challenge of the Council's MTFS process and projections. The review was not commissioned because of any underlying concern with the MTFS process or the consequential budget and savings plans, which were approved by Council on March 5th. It was commissioned as a high level review (of the main numbers and issues, not a detailed audit of the model, its assumptions and the savings proposals) to assure the Council that the model was reliable and that the savings identified were reasonable in the context of the financial gap. The resource budget for the review was agreed at ten days to review and test:

- The logic of the Council's MTFS
- The reasonableness of assumptions underlying the budget savings figures and construction of the budget (inflation rate pressures, pay awards, demographic changes)
- The budget savings programme for the next five years
- The approach to reserves (both general and earmarked reserves) and provisions.

The independent finance professional was also asked, as a result of his work with WCC and other authorities, to offer suggestions on:

- Areas of the budget that could release further savings
- Ideas where the Council might learn from other councils or public sector bodies.

Methodology

The review was conducted using a combination of personal interviews with key Councillors and officers, plus External and Internal Audit (see Appendix A). I reviewed all relevant papers including the last three iterations of the MTFS (and supporting assumptions and spreadsheets), papers on reserves, Treasury Management and Minimum Revenue Provision. I also read the External Audit Review of the MTFS process dated September 2013.

As requested by the Council, my approach has been challenging, inquisitive and robust.

Acknowledgements

I am grateful to all the people listed on Appendix A who willingly and helpfully spared the time to meet me. Their contribution has helped shape my conclusions, which are entirely my own. I owe special thanks to two people. Nick Alderman, Chief Accountant, was very helpful in producing additional spreadsheets which I requested. He also helped with challenge or corroboration of my interpretation. Karon Brood, Personal Asst to Asst Director, Delivery, was also very helpful in the logistics of this review in terms of diary commitments, office accommodation and facilities.

CONCLUSIONS AND RECOMMENDATIONS

Overview

In drawing my conclusions and recommendations, it is not my wish to criticise the Council or its processes for the MTFS. I remain of the view that its approach to five year planning is as good as I've seen anywhere else. There is a thorough approach to identifying assumptions and making reasonable (not optimistic or pessimistic assumptions) for the next five years. The financial reports which go to Cabinet are well constructed, well drafted and make good use of narrative, tables and graphics.

I have no doubts about the overall accuracy painted by the MTFS model and accompanying reports. The gap between likely revenues (which are forecast to drop) and future spending does not look exaggerated, especially as costs continue to rise with pay and cost pressures and with demographic demand in certain key areas such as Adults Social Care and Looked After Children.

The impact of certain assumptions may prove to be wrong when looked at in retrospect but that is the nature of trying to predict the future. I would not wish to supplant any of the assumptions with alternative suggestions.

Nevertheless I have been encouraged to be challenging, inquisitive and robust. With that mindset I have some reservations about whether the MTFS is more helpful to those who are close to it and own its conclusions than it is to those who are further away from it and are faced with accepting the results without fully understanding or believing them.

I know that Chief Officers and many Councillors will be close to these issues and fully understand them. But I wonder how many interested parties really understand and could explain why a £97.5 million gap over five years in October 2013 became £123 million by January 2014. And why in February 2014, after identifying savings of £65.5 million, the Council still needed to find another £59.2 million.

The remainder of my report covers:

- The MTFS model and four measures to help Councillors to have informed confidence in the model, understand and believe in it and its results. The four main measures are (1) confidence in the model itself, (2) ownership of the assumptions, (3) understanding and believing the results of the model, and (4) due diligence

- I offer two reasons why there is a risk that some Councillors, other interested parties and the public, who are not close to the budget and/or local government finance, may find the model and its messages hard to understand and believe. I also offer approaches which may help
- I comment on the inter-relationship of the key elements of a financial strategy including spending plans, corporate revenue (Revenue Support Grant, Council Tax and others), Fees and Charges, and Reserves
- I offer the view that Fees and Charges are not being given sufficient weight in the overall financial strategy
- I note the Council has a good grasp on the importance and limitations of reserves as part of the financial strategy
- Finally, I address the issues about possible other areas for savings and ideas from elsewhere.

MTFS – The Model

In advance of my first meeting with Chief Officers, I had read several background papers including the last three MTFS reports to Cabinet. My initial impression, based on my background reading of the MTFS reports and related papers, was that the approach by WCC looked exemplary and was among the best I've seen. I remain of that view after my interviews and further research. The approach is in line with good practice and encompasses:

- Medium term financial planning covering the next 5 years
- Regular updates and reports to Councillors
- Savings plans identified, agreed and profiled over the five year period to reflect when savings will be achieved
- The residual gap between available resources and spending plans – for the whole five years, with each year separately identified
- Annual reviews of the level and purpose of reserves (including earmarked reserves) and provisions
- Detailed savings plans by Cabinet portfolio
- Evidence of a reasonable track record on delivering against intentions but inevitably some areas where plans are not fully achieved or were used to address overspending elsewhere.

Even with the above good practice, I believe Councillors, and possibly some Chief Officers, need greater support to help them understand and believe what they are being told. In general, Medium Term Financial Strategy models are by their nature complex and there is a risk that within WCC (and across many authorities) some officers and some Councillors may be relying on trust that the model is reliable and it has been used correctly. In particular WCC should consider four measures to support Councillors and create:

- Confidence in the computer model itself
- Ownership of the assumptions which under pin the projections
- Understanding and belief in the financial results of the model in terms of the main factors which create significant shifts in expenditure plans and available resources
- Assurance for big decisions using independent due diligence reviews.

Confidence in the Model

Within the time available for this review I was not expected to do an audit of the model, the assumptions, the inputs and outputs. However I did consider whether there is good reason for Councillors and Chief Officers to have confidence in the actual model. It has been reviewed by the external auditors and they are satisfied that it is a sound and prudent basis for financial planning. I also spoke to Internal Audit and they raised no concerns about the MTFS model. I have spoken to several people within the Council (officers and Councillors) and none has raised a doubt about the model.

I have reviewed the reports and the spreadsheets. I have sought explanations from Nick Alderman, Chief Accountant. His explanations are always clear, credible and coherent. I have also requested analyses and spreadsheets from certain parts of the model. These have always been produced quickly and are consistent with the main numbers reported by the model. For these reasons, it is reasonable for me to have confidence in the model.

However models tend to get amended over time. Sometimes new assumptions or formulae need to be added or a formula overwritten. Version control is important but these amendments are relatively easy for someone with good spreadsheet skills. There is a risk that such changes can be uncontrolled and human error undetected. Basic errors can creep in such as using a plus instead of a minus, or vice versa, transcribing errors, or wrong cell references. The risk of such errors can be quite high. I have no reason to suspect that any of these risks have crystallised and been left uncorrected. It is more likely that any material errors would be reflected in the results and are likely to be detected because of an unexpected and unexplained material movement in the figures. However the MTFS is the cornerstone of the Council's overall strategy and the basis for major decisions on future services, pay and jobs. Confidence in the model must be assured not assumed.

RECOMMENDATION 1: I recommend a full assurance review of the MTFS model by Internal or external audit in advance of next year's budget setting process.

Own the Assumptions

All medium term financial planning models depend on assumptions about (a) what may happen in the future and (b) the impact of each assumption on income or expenditure. Within the WCC, assumptions are grouped under five main headings:

- Demand changes
- Inflationary pressures on pay (and pensions)
- Inflationary pressures on goods and services including utilities
- Income sources (for WCC this is mainly Revenue Support Grant, Council Tax, Business Rates and Fees and Charges)
- Treasury Management (assumptions about interest charges, debt levels, Capital requirements).

In WCC these assumptions in the MTFS fall into two broad categories:

- General assumptions affecting a range of costs or derived from national data e.g. inflation (see Appendix B for detail of WCC general assumptions)
- Specific assumptions which impact single areas of income and expenditure and are based upon local data (see Appendix C for detail of WCC specific assumptions).

As with any assumptions about the future, there is a degree of uncertainty inherent in the process. For example, even in the age of austerity, there is an expectation that pay and prices will continue to rise. The modelling challenge is deciding ‘how much’ in each of the next 5 years.

Most models allow for alternative scenarios to be modelled and usually include assumptions which are (a) pessimistic (b) realistic or (c) optimistic. Public sector finance is based on the concept of prudence with public money. Optimistic assumptions can prove reckless, leaving the Council insolvent, and pessimistic assumptions could drive the Council to take unnecessary action which adversely affects service users, council tax payers and employees. For those reasons it is important that the Council is neither optimistic nor pessimistic about future assumptions.

I think more could be done to extend the understanding and ownership of the assumptions beyond the Finance Team to other Chief Officers and Councillors.

RECOMMENDATION 2: I recommend that formal approval of the assumptions, including any future changes when they arise, should include the financial implication of each assumption.

Understand and Believe the Results

It is logical that if officers and Councillors have confidence in the model and approve the assumptions, then they will also own the results. However part of owning the results is the ability to understand and believe the individual causes behind them and the full impact of key assumptions.

The WCC approach to MTFS makes it harder for non financial experts to own the results. The MTFS reports are very thorough and well written. However they are long and technical and more accessible to those who are financially literate. Someone who was not financially literate would understand the gravity of the situation but not necessarily the reasons for it. This is partly because the MTFS is regularly updated and there can be significant movements between reports. For example the five year spending gap rose by £25.46 million between October and January. This was reported to Cabinet on 8 January and explained in paragraph 2.2, Table 1, Appendix A and Appendix B of that report. I am not sure it is easy for all Councillors to convert that information into a clear narrative. It is also quite difficult for Councillors to work out the full five year effect of the latest assumptions because sometimes they are expressed as movements since earlier reports.

In my view there are two related problems which may make it hard for Councillors, other interested parties and the public, who are not close to the budget and/or local government finance, to both understand and accept the nature and scale of the challenge. The first is stakeholders face a moving target occasioned by in year updates of the five year financial strategy. This may have been necessary because of the frequency and timing of changes to assumptions but it can be hard for Councillors outside of Cabinet (Resources) Panel. The second is the tendency to quote total figures for the five years without contextualising that as an average per annum or percentage of total budget. For most people in public life the natural response to challenges is to take on those that are very hard but doable (in the best interests of the public). The risk is when the challenge feels impossible the natural response can be to refuse to engage with the challenge (and for some that can be seen in the best interests of the public).

For example finding a further £25.46 million sounds very daunting for Councillors when the Council has only just recently found two-thirds of the £97.56 million required. However it may not seem so daunting if converted to an annual savings requirement and shown as a percentage of the annual budget.

RECOMMENDATION 3: I recommend:

- **One iteration of the five year projections (around October or November) in advance of setting the budget for the coming year (unless there are major changes to the figures which require urgent consideration)**
- **In-year monitoring of the financial budget for the current year, possibly with a future trends paragraph which might alert Councillors to anything material which might affect future plans**
- **Maintaining the financial model as a live model for S151 and management purposes.**
- **Telling the story and the financial strategy in a way that makes the scale of the challenge clear and unequivocal but achievable with focus and commitment to a common purpose.**
- **Shortening and simplifying budget and financial outturn and strategy reports with financial data and detailed commentary moved to appendices wherever possible to provide greater clarity.**

Due Diligence

Sometimes it is not sufficient to have confidence in the model, own the assumptions and understand the results. The MTFS, the coming year budget and the key savings proposals are all major decisions for the Council. In most organisations, including local authorities, it is normal, in advance of major decisions, to commission a due diligence review.

The essence of due diligence is to commission a review by an independent professional to give a view on the information being presented 'Is it a suitable basis on which to make a decision?'. Independent does not necessarily mean external although that additional level of independence can be seen as more robust.

RECOMMENDATION 4: I recommend that the Finance Department should arrange a suitable and proportionate annual due diligence review (possibly by internal or external audit) to append to its MTFS report to Cabinet.

Fees and Charges

Notwithstanding my comments about the model following good practice, I am not convinced that the Council is properly considering Fees and Charges within its Medium Term Financial Strategy. In Appendix D I set out a summarised approach to determining a MTFS strategy around four main financial elements (A) Spending Plans (B) Revenues from Council Tax, RSG and NNDR (C) Fees and Charges and (D) Use of reserves.

WCC has all of these elements in place, except it does not seem to embrace Fees and Charges as part of its financial strategy. This is surprising given the annual income deriving from such fees (£66 million in 2013/14 – compared to £70 million in 2012/13). The Council regularly reviews the level of fees and charges, and the budgets for fees and charges are within the MTFS. However it does not appear to receive strategic advice on the impact of the level of fees and charges on the total sum that might be raised at given levels level of fees or on its overall approach to income generation. I understand the LGA has a web based resource which might be helpful http://www.local.gov.uk/income-generation.

It is surprising that there is not more scrutiny of the overall importance of Fees and Charges to the MTFS and that charging levels are considered after the budget has been set. In particular the setting of fees and charges does not consider the overall level of income derived from individual charges but focuses on the absolute level of each charge. This, in itself, can lead to undue attention being given to items of lower importance at the expense of a more holistic and strategic view.

RECOMMENDATION 5: I recommend that there should be:

- **greater modelling and economic focus on not just the charge for a service but also the anticipated level of income that might be raised**
- **an explicit focus on fees and charges/income generation in the MTFS**
- **a determination of the fees and charges for the coming year before or when setting the budget.**

Reserves

The Council's reserves can and have been used as part of its MTFS provided they are **only** used to:

- fund a non recurring gap
- or fund a recurring gap for a finite period until a expenditure plans and revenues are brought into balance.

The Council has a clear policy on the minimum level of its level of general reserves which have recently been set at £10 million. The minimum level was adjusted downwards from £15 million to £10 million as part of the October budget setting report following an assessment of the general level of reserves and budget risks by the S151 Officer. The risk assessment noted that there was a reduction in several key budget uncertainties:

- Single status – settlements to be largely resolved in 2013/14
- Equal pay – settlements progressing and uncertainty reduced
- Pay aggregation – HMRC claim has been resolved with nil payment.

Based on these and the overall level of reserves it was assessed that the minimum level of general balance could be reduced. The S151 Officer assessed a prudent reasonable level at £10 million. This level equates to some 4% of net expenditure which is midway in the "unofficial standard" of 3-5% (as noted in the 2012 Audit Commission report on reserves).

The Council also regularly reviews the level of its earmarked reserves and releases them when prudent to do so. There is some limited scope to review earmarked reserves again, with a more stringent approach to identifying what could be released if absolutely necessary; for example, in order to avoid issuing a Section 114 notice. Council Finance Officers assess this scope at a maximum of £12 million. However Council Finance Officers would not recommend using that scope because there would be no contingency left for any unforeseen circumstances (for example this figure includes eliminating the insurance reserve to cover self-insured risks) or slippage in the savings programme. I agree it would not be prudent to reduce earmarked reserves at this time.

It is worthy of note that the revised projected budget deficit for 2014/15 is almost £12 million, subject to identifying further savings plans for 2014/15. The Council's reserves need to be protected as mitigation against any slippage in plans and/or any unforeseeable events.

RECOMMENDATION 6: I recommend current earmarked reserves are preserved as mitigation against any unforeseen pressures in 2014/15.

Challenge to the Budget

The legal framework builds in certain duties on Local Authority Officers and their External Auditors to safeguard against wilful or reckless action by Officers or Councillors. The 1998 Local Government Finance Act, S114(3), is particularly relevant to the duties of the

Section 151 Officer: 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.

There is also a duty on the External Auditor under Section 19 (a) of the Audit Commission Act 1998. He may issue a notice under this section (an advisory notice) if he has reason to believe that the body or an officer of the body:

- is about to make or has made a decision which involves or is likely to involve the body incurring expenditure which is unlawful
- is about to take or has already taken a course of action which, if pursued to its conclusion, would be unlawful and likely to cause a loss or deficiency, or
- is about to enter an item of account, the entry of which is unlawful.

It is a matter for those charged with those duties to decide when and what circumstances to exercise their duty. The budget for 2014/15 has been set and neither party (to the best of my knowledge) has exercised their duty under these clauses. It would appear unlikely that this will apply during 2014/15 unless there is significant in-year budget movement which might trigger their action.

RECOMMENDATION 7: I recommend the Council seeks further clarification from each party as to the triggers for action under these clauses and the process which might follow.

Areas of the Budget that Could Release Further Savings

I was asked to consider whether there were other areas where the Council might release further savings. I offer the following thoughts knowing the Council has already considered (and implemented) some or all them if and will do so again if and when the circumstances are right. The ideas in the current savings plans show the thoroughness of the Council's approach to its savings plans.

In offering these ideas I am not identifying whether I have any special advisory expertise in these areas which would help the Council and I am not offering the suggestions in the hope that I may be offered more work with the Council. I would be prepared to discuss the ideas with officers or Councillors if requested but I would be reluctant to confuse my independent role and any advisory role.

Savings Strategy

The Council has 205 savings ideas in its total savings plan of £65.5 million with 30% due in Year 1. These projects are grouped into programme areas wherever possible and it is important that Executive Directors individually and collectively take responsibility for delivery on these plans and report progress to appropriate that Elected Member meetings. It is important that Councillors are resolute in their continuing support for the measures which will bring the Council's spending plans and resources into balance on a recurring basis. (I understand that about 18 of the projects account for about half of the first year's savings. Executive Directors and Councillors need to closely monitor the large individual projects as well as the overall control total for the year.

In my experience savings projects often fall into three main categories:

- significant corporate and cross cutting projects which are strategically important in their own right and which require close corporate attention
- smaller self contained projects which are owned by a Director or budget holder who is committed to its achievement and to be held to account for it
- good housekeeping – the management of pay and non pay budgets which every budget holder should be held to account for without having to stipulate how it will be achieved and without having to produce monitoring reports to show the progress being made – because the saving is top sliced off their budget and they are held to account for it through budget monitoring. I would suggest a percentage of their budget say 1-2%. If adopted this would instantly transfer some or all of the extra £25.46 million from the need to identify savings ideas into a budget management challenge around good housekeeping. The essence of this approach is ownership by the budget holders who might prefer this delegated responsibility over the challenge of identifying and managing more savings plans.

Minimum Revenue Provision

The Council's Minimum Revenue Provision is £39.9 million, including an HRA provision of £14.3 million. This figure looks high at 5.5% of the Council's Capital Financing Requirement.

The Council's Officers are already aware of the importance of the Minimum Revenue provision and have been considering the potential to release part of the provision. I understand that the Council is in discussions with the External Auditors about approval for a possible change. I am not aware of the detail of the proposed change.

Debt Recovery

I have not looked into the detail but I am aware that the Council may have some old debts particularly in Adult Social Care. Experience elsewhere has shown that Council's can accumulate debts as a result of focusing too much attention on raising the charges and not enough on collection. Old debts are notoriously difficult to collect but experience has also shown that a focused collection and recovery team can produce good results if they analyse the debtors well and target their efforts on those with prospects for collection.

Discretionary Services

I acknowledge the importance to the community, and to the users, of discretionary services. Nevertheless these services can sometimes place a financial burden on the Council which forces it to consider difficult choices. These services can include Libraries, Leisure Centres and Civic Theatres which incur subsidy.

I know from my discussions that Chief Officers and Councillors are willing to consider options for reducing or eliminating council taxpayer subsidy alongside other options for saving money.

Asset Disposal

Asset disposal is also something worthy of consideration and I know it is in included in the Council's thinking. The Council owns several assets, some of which may be tied up in discretionary subsidised services. Taking a view of options which involve removal of subsidy and disposal of the asset may create wider opportunities.

NB: All of these measures involve making choices. The key to good choices is to obtain and focus on relevant information, ignore irrelevant information and make an informed choice.

Ideas where the Council might learn from other councils or public sector bodies

Benchmarking

As a diagnostic tool the Council could usefully use the Audit Commission Profiles to identify areas where the Council's costs and performance do not, at first glance, compare favourably with its comparator authorities. Thereafter the Council may find areas of difference which are worthy of further investigation to identify causes.

Sharing with Neighbouring Authorities

There are undoubtedly opportunities for all councils to share with their neighbours and there are an increasing number of examples of councils willing to consider doing this. However such sharing is not without its difficulties and often there is not enough commitment to a common purpose and the difficulties can become insuperable or not worth the effort. There is even the risk of significant waste of time and money and the concept falls apart because of a lack of consensus. Therefore options for sharing, and partners, should be chosen with care.

The Council should, as I know it is, be open to sharing initiatives, where there is good will and a genuine commitment from another authority to make it work.

Sharing With Other Bodies in Wolverhampton

The same principle applies to other public, or private, bodies within the City. The most likely common purpose would relate to shared services arrangements for common functions such as HR, Payroll, Facilities and others. However the prize must be worth the effort and the risk of successfully implementing a sharing arrangement. Potential candidates for such sharing would include Higher Education, Further Education and NHS. The NHS may be more logical partners for many things with the advent of the Better Care Fund and NHS England's commitment to strengthening local health economies, in conjunction with Local Health and Wellbeing Boards.

Commissioning

There are some who argue that the duty of a council is to commission services for its residents and users and not necessarily to be the provider of the service. There are models of this across the country. In such an arrangement the Council would seek bids from a suitable provider of services against a specification and contract which ensured delivery and quality to secure payment, including the possibility of a 'payment by results' contract.

There are logistical, political, organisational and people issues implicit in such a choice. However the benefits can be considerable (often across all four of those issues) and more certain than other reconfiguration options.

I am aware that the Council has recently approved a significant procurement and outsourcing programme. The independent business case to support this programme highlights procurement is the most certain route to achieve the highest savings. It is important for Officers and Councillors to maintain the timetable for this procurement to maximise the savings.

Eugene Sullivan, CPFA (Hons) 30 May 2014 (Amended 11 July 2014)

APPENDIX A

Interviews and Documents

Interviewees:

Councillor Roger Lawrence – Leader of the Council
Councillor Andrew Johnson – Cabinet Member for Resources
Keith Ireland – Strategic Director Delivery
Sarah Norman – Strategic Director Community
Tim Johnson – Strategic Director Education and Enterprise
Mark Taylor – Assistant Director Finance
Nick Alderman – Chief Accountant
Peter Farrow – Head of Audit
Richard Vialard/Richard Bacon – PwC

Documents Supplied:

Community Directorate – Summary of Savings Plans 2014-19
Wolverhampton Labour Budget Message Card
Cabinet – 25/2/14 – Treasury Management Strategy 2014/15
Cabinet – 26/2/13 – Treasury Management Strategy 2013/14
Cabinet (Resources) Panel – 11/3/14 – Fees and Charges Review 2014/15
Cabinet - 25/2/14 – Five Year Budget and Medium Term Financial Strategy 2014/15 to 2018/19
Cabinet – 4/3/14 – Deloitte LLP – In-house Service Options Appraisal
Specific Reserves Working Group – 16/1/14 – Review of Specific Reserves
Cabinet – 25/2/14 – Capital Programme 2013/14 to 2017/18 Quarter Three Review and 2014/15 to 2018/19 Budget Strategy
Cabinet (Resources) Panel – 11/3/14 - Revenue Budget Monitoring 2013/14 Quarter Three
Cabinet – 24/7/13 – Reserves, Provisions and Balances 2012/13
Cabinet – 24/7/13 – Draft Budget Strategy 2014/15 and Medium Term Financial Strategy
Cabinet – 23/10/13 – Five Year Budget and Medium Term Financial Strategy 2014/15 to 2018/19
Cabinet – 8/1/14 – Five Year Budget and Medium Term Financial Strategy 2014/15 To 2018/19

APPENDIX B

Budget and MTFS Assumptions

General Assumptions

General assumptions are as listed in and Appendix D to the budget report to Cabinet and are attached to this document.

The basis for these is as follows:

Council Tax Increases: 2% annually as per current referendum limit

Council Tax Base: 0.5% annual growth in line with recent new build data and with the New Homes Bonus estimates

Cost price inflation (excl. utilities and NNDR): 0% as it is assumed that all costs will remain flat with improved procurement offsetting any inflationary pressures

Cost price inflation – Gas: 5.7% annually, based on recent trends.

Cost price inflation – Electricity: 2.5% annually, based on recent trends.

Cost price inflation – NNDR: 3.9% set at 2013 RPI level as although capped at 2% the difference is to be funded by Central Government. Based upon current inflation rates this rate may need revisiting and reducing in future iterations to reduce inflation level.

Growth in NNDR tax base – 0.1% for 14/15, 0.2% thereafter. Little growth as experienced in recent trends in local economy.

Increase in Top-up grant – 2.0% in 14/15, 3% in 15/16, 4% in 16/17 & 17/18, 0% in 18/19. These are uprated annually by the increase in the small business rates multiplier (previously by inflation). 14/15 and 15/16 are based on the settlement figures. Thereafter on estimates that will be reviewed on MTFS refresh – risk is to the downside.

Decrease in RSG – reductions for 14/15 and 15/16 of 16.9% and 29.2% reflect the settlement figures. Reductions thereafter are predicated on further cuts in Government spending (as confirmed by the chancellor further £25 billion in the next spending round). Reductions are in line with the LGA projections and comparable with local equivalents although some forecasts put the reductions far greater. Balanced risk based on current knowledge.

APPENDIX C

Budget and MTFS Assumptions

Specific Assumptions

The following are the significant specific income/expenditure assumptions made in the budget and MTFS. Apart from the specific growth elements identified below there are no other predicted growth in expenditure arising from specific cost pressures.

New Homes Bonus - estimated based upon new build forecast data supplied by the strategic planning department. The figures are slightly greater than those recently achieved. This data has also been fed in to the tax base data to ensure consistency. The NHB adjustment grant has been calculated based upon the LG Futures forecast of the national new homes bonus calculations.

Fees & Charges – no increase in fees and charges has been budgeted as the agreed figures were not available when the budget was prepared. Fees and charges have been analysed separately for review.

Looked after Children – an increase over the 2013/14 base budget of £7.5 million has been included to bring expenditure up to current levels (£2.5 million of this held separately as a corporate contingency). Numbers are continuing to rise and there is a potential downside risk.

Adult Social Care – growth of £2 million per annum has been included, although from 2015/16 onwards this is assumed as met from the Better Care Fund (i.e. net growth of £nil). This growth is based on a forecast prepared by LG Futures for Wolverhampton showing demographic growth of c. £400,000 per annum together with internally calculated additional transition costs (young people transitioning to the adult care system) of £1.1 million. The balance of £0.5 million is to fund other growth pressures in the service.

Care Bill – there is no growth reflected in the budget/MTFS for additional costs arising from the Care Bill. At the time of preparation these were unquantified and assumed to be met by additional funding. The costs have now been estimated at £2.5-£3.0 million in the first year (2016/17) rising to £4 million per annum over the medium term. The funding for these additional costs is not yet clear but is a significant downside risk.

APPENDIX D

Approach to Setting a Medium Term Strategy

The Medium Term Financial Strategy is always a balance between the spending plans and the resources available to fund it. It is prudent also to consider the going concern issue and therefore plan to have a positive balance sheet, including cash and short term liquid assets. It is not easy to get the balance right and it is important to control those things which you can control. The basic approach is to determine:

- **A** - How much will be spent on providing current and future services bearing in mind both price and demand growth. The Council is not wholly in control of this figure because there are things which must be done (statutory) and things that are desirable do (discretionary). Most Council's are forecasting increased demand in the statutory areas of Adult Social Care and Looked after Children. Expenditure plans are further complicated by the fact that the Council may be able to influence future levels of spend by managing demand and/or altering delivery mechanisms – but need time to change or transform the ways services are currently configured and provided
- **B** - How much resource can be raised from statutory sources Council Tax, Grants, NNDR
- **C** - How much can be raised from Fees and Charges (a complex matter in which the Council can control the level of the charge but cannot control demand – and for some services increased charges will adversely affect demand
- **D** – Use of reserves

If A is greater than the sum of B and C (after the Council is satisfied that none of the figures can be realistically or prudently improved) then the Council has an 'expenditure gap'. If the gap is recurring action needs to take action to bring income and expenditure into balance as quickly as possible. If that can't be done within the financial year the Council will need to use reserves (D) where available – but this must always be seen as a measure which only buys time to find sustainable solutions. It is not a sustainable solution in itself.

The plan which brings expenditure plans and resources into balance is called different things - a savings strategy, improvement programme or cost reduction programme. It is crucial that the savings strategy is realistic and is properly managed and profiled to ensure the delivery of the plan.

Independent review of process for medium term financial strategy and budget
Action Plan to Implement Recommendations

Recommendation	Action	Responsible	Date
1. A full assurance review of the MTFS model by Internal or external audit should be undertaken in advance of next year's budget setting process	Internal audit to undertake assurance review of MTFS model	Head of Audit	30 September 2014 and then annually
2. Formal approval of the assumptions, including any future changes when they arise, should include the financial implication of each assumption.	Formal approval of assumption is already sought, this will however be enhanced and included in the October budget report to Cabinet, in order to make even clearer what has changed and what this impact was.	Chief Accountant	31 October 2014 and then ongoing

Recommendation	Action	Responsible	Date
3. Only one iteration of the five year projections (around October or November) should be reported to Councillors in advance of setting the budget for the coming year (unless there are major changes to the figures which require urgent consideration)	The five year projections will remain under constant review and all reports will make reference to the extent of the challenge over the five year period, the main focus will however be on the following financial year. This will ensure that that Councillors are able to make fully informed medium term focussed decisions. The number of iterations of the five year projections that are reported will depend on the significance of the changes between each reporting period.	Chief Accountant	31 October 2014 and then ongoing
4. In-year monitoring of the financial budget for the current year should also possibly include a future trends paragraph which might alert Councillors to anything material which might affect future plans	Quarterly monitoring reports will continue to focus upon the current financial year with a future trends paragraph included where and when appropriate	Chief Accountant	31 July 2014 and then ongoing
5. The financial model should be maintained as a live model for the Section 151 Officer and management purposes	The MTFS will continue to be maintained as a live model with regular updates provided to the Section 151 Officer	Chief Accountant	Ongoing

Recommendation	Action	Responsible	Date
6. The story and the financial strategy should be told in a way that makes the scale of the challenge clear and unequivocal but achievable with focus and commitment to a common purpose.	Templates for reports and presentations will be reviewed, Communications and Democratic Services colleagues will be consulted as part of this review in order to ensure that the key messages and actions are communicated as clearly as possible This has already been actioned for the 25 June 2014 Cabinet report.	Chief Accountant	31 July 2014 and then ongoing
7. Budget and financial outturn and strategy reports should be shortened and simplified, with financial data and detailed commentary moved to appendices wherever possible to provide greater clarity.	Templates for reports and presentations will be reviewed, Communications and Democratic Services colleagues will be consulted as part of this review in order to ensure that the key messages and actions are communicated as clearly as possible This has already been actioned for the 25 June 2014 Cabinet report.	Chief Accountant	31 July 2014 and then ongoing
8. The Finance Department should arrange a suitable and proportionate annual due diligence review (possibly by internal or external audit) to append to its MTFS report to Cabinet.	Due diligence review to be undertaken annually by internal audit to validate methodology and assumptions used	Head of Audit	December 2014 and then annually

Recommendation	Action	Responsible	Date
9. For fees and charges there should be: • greater modelling and economic focus on not just the charge for a service but also the anticipated level of income that might be raised • an explicit focus on fees and charges/income generation in the MTFS • a determination of the fees and charges for the coming year before or when setting the budget.	Fees and charges to be set prior to the final budget being reported to Cabinet during February each year. The process will include volume/demand modelling in significant areas as well as consideration of the absolute level of income generated	Chief Accountant	December 2014 and then annually
10. Current earmarked reserves should be preserved as mitigation against any unforeseen pressures in 2014/15.	At the end of 2013/14 earmarked reserves were higher than had been projected during the year, this will be formally reported to Cabinet in July. Earmarked reserves will continue to be reviewed on a regular basis, including an annual review by Scrutiny, in order to ensure that what is being held is both robust and prudent.	Chief Accountant	Ongoing
11. The Council should seek further clarification from the Section 151 Officer and the External Auditor as to the triggers for action under relating to Section 114 and Section 19 powers.	Section 151 Officer and External Auditor to discuss and document the triggers before reporting to Senior Management and Councillors	Assistant Director Finance	31 July 2014