

<b>REPORT REFERENCE NO.</b>	<b>APRC/22/11</b>
<b>MEETING</b>	<b>AUDIT AND GOVERNANCE COMMITTEE</b>
<b>DATE OF MEETING</b>	<b>22 JULY 2022</b>
<b>SUBJECT OF REPORT</b>	<b>GOING CONCERN REVIEW</b>
<b>LEAD OFFICER</b>	<b>DIRECTOR OF FINANCE, PEOPLE &amp; ESTATES (TREASURER)</b>
<b>RECOMMENDATIONS</b>	<i>That the report be noted.</i>
<b>EXECUTIVE SUMMARY</b>	<p>The Authority's External Auditors have requested a formal response from management over the ability of the Authority to continue as a going concern.</p> <p>This is the fourth such report which has been prepared and contains a review of the financial position as at 31 March 2022 alongside an assessment of the ability of the Authority to continue operating for the foreseeable future.</p> <p>As we move out of the COVID-19 pandemic, it is probable the recovery will have a significant impact on financial risk in the coming years but the Authority is well placed to respond to these.</p>
<b>RESOURCE IMPLICATIONS</b>	As indicated within this report.
<b>EQUALITY RISKS AND BENEFITS ANALYSIS</b>	N/A
<b>APPENDICES</b>	None
<b>BACKGROUND PAPERS</b>	<a href="#">Report AGC/22/4 (Draft 2021-22 Annual Statement of Assurance)</a> and the <a href="#">Appendix to that report</a> as submitted to the Committee meeting held on 10 May 2022.

## **1. INTRODUCTION AND BACKGROUND**

- 1.1. Under International Audit Standards auditors are required to “obtain sufficient appropriate audit evidence regarding, and conclude on, the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements”, and to conclude, based on the audit evidence obtained, whether a material uncertainty exists about the entity's ability to continue as a going concern.
- 1.2. This report is the fourth such report made to the Audit and Performance Review Committee and will consider the Authority’s ability to continue as a “Going Concern” i.e. to deliver its functions and services for the foreseeable future, particularly focussing on the 12 month period following the Statement of Accounts balance sheet date of 31 March 2022.
- 1.3. The sustained period of Austerity since 2010 and resulting reductions to funding across Local Government now pose a significant threat to public sector organisations. As a consequence, the External Auditors, Grant Thornton LLP, are placing greater emphasis on the Authority’s ability to continue as a Going Concern. There have also been several high profile cases of Local Authorities struggling to meet their financial and service delivery obligations which makes the ability to continue as a Going Concern of greater relevance. The COVID-19 Pandemic has had a significant impact on public sector finances and the Authority as a whole. This is covered in more detail below.

## **2. GOING CONCERN REVIEW**

- 2.1. This report will consider the following factors which underpin the Authority’s ability to operate as a going concern:
  - (a) The current financial position;
  - (b) The projected financial position;
  - (c) The balance sheet and Cash Flow;
  - (d) Governance Arrangements; and
  - (e) The regulatory and control environment.
- 2.2. Each of these elements will be considered in greater detail in the following sections.

## **3. THE CURRENT FINANCIAL POSITION**

- 3.1. Total revenue spending in 2021-22 was £75.601m compared to an agreed budget of £74.222m, resulting in an overspend of £1.379m, equivalent to 1.86% of total budget. To ensure the revenue position was balanced at year-end, it was necessary to use reserves. A review was also undertaken of provisions held for bad debt and pensions which were also reduced to assist with the overspend position.

- 3.2. The Authority has previously delivered, consistently, underspends against the Revenue Budget and has therefore built-up Earmarked Reserves of £31.759m and General Reserves of £4.050m as at 31 March 2022. The strategy for use of those reserves and adequacy of the general fund is outlined in the Authority's Reserves Strategy which was reviewed and approved by the Authority on 29 September 2021. The next iteration of this is in development and will be presented to the Resources Committee at its forthcoming meeting. The risk assessment of the general fund offers assurance that the Authority will be able to cover any unforeseen liabilities in the short to medium term.
- 3.3. The Authority has set a balanced budget for 2022-23 of £77.289m with £1.665m planned use of Reserves in respect of grants received in advance of need. On top of this, £1.244m of the Capital Reserve has been utilised to invest in new equipment and Included within the On top of this, £1.302m has been drawn from some of the Reserves held specifically to assist in funding future year's budgets. At this early stage in the financial year, forecasts suggest that spending will be £1.2M greater than the agreed budget figure. Plans are in train with managers to reduce discretionary spend where appropriate, coupled with a temporary slow-down of recruitment which is felt will ensure the budget is balanced at year-end with no further depletion of Reserves to support revenue expenditure.
- 3.4. The Authority's main sources of funding are Council Tax and Business Rates income and central government grant funding. Levels of funding are agreed and set as part of the budget setting process which offers a guarantee that the income will be received for 2022-23. Any adjustments to Council Tax and Business Rates income are made via the collection fund budgeting process so will impact on future years.
- 3.5. Because there is surety of funding from billing authorities and central government, the main area of risk to the short term financial position of the Authority is its ability to control expenditure. There are robust financial monitoring processes in place to review spend against budget, with reports presented monthly to the Executive Board and quarterly to the Resources Committee.

#### **4. THE PROJECTED FINANCIAL POSITION**

##### ***Revenue Budgets***

- 4.1. As outlined above, the predicted financial position for 2022-23 as year-end is for spend to be within the revenue budget. Expenditure from reserves is anticipated to be £11.7m within the financial year with projected balances of circa £22.0m at year-end.
- 4.2. In considering its annual budget requirement, the Authority reviews the Medium Term Financial Plan (MTFP). In February 2022, a potential funding gap of between £10.1m and £12.4m was identified as shown in the chart overleaf. In order to close the funding gap, significant savings will need to be identified, the Authority's change programme, has been tasked with finding efficiencies along with potential changes to progress towards a model which will fit future funding.



- 4.3. The Authority has published its Medium Term Financial Plan, which articulates the basis of the forecast, funding scenarios and the assumptions made. The Medium Term Financial Plan covers the five year period to 2025-26.
- 4.4. Until further information is available to inform financial strategy such as flexibility to increase the Precept by more than the current 1.99%, new targets cannot be established. However, the Authority has sufficient reserves which could be repurposed over the medium term to fund budget gaps. This is not a sustainable long-term solution. Going forwards, the Authority will need to reconsider savings programmes.
- 4.5. One of the current concerns to the Authority is inflation. The 2022-23 revenue budget was built with an assumption of 2% inflation on all items, including payroll except for energy which was presenting large increases by February 2022 when the budget was agreed. The Consumer Price Index (CPI) increased by over 9% in June, with forecasts suggesting that it will increase further. This will impact on the already stretched budgets.

### **Capital Budgets**

- 4.6. Capital Budgets are set annually by the Authority as part of the budget setting process and are published alongside an indicative programme for the following three financial years. Funding requirements are identified as part of that planning cycle and for 2022-23 consist of a Revenue Contribution of £0.300m, Application of Existing Borrowing of £1.365m, Capital Receipts of £0.300m and use of Earmarked Reserves of £5.089m.
- 4.7. In considering the Capital Programme over a longer time period, a healthy earmarked reserve of £12.3m is anticipated to be available for 2023-24 and beyond. However, the need to progress assets following a pause in replacement means that the Authority may need to borrow in 2024/25. There is sufficient funding to support capital expenditure in the short term with a need to rationalise assets if the programme is to be accelerated.
- 4.8. The long-term strategy of the Authority is to fully support the Capital programme through Revenue Contributions. This is going to prove to be a challenge given the size of the current capital programme coupled with the pressure on the revenue budget.

## **5. THE BALANCE SHEET AND CASH FLOW**

### ***Balance Sheet Review***

- 5.1. The draft unaudited Financial Statements of the Authority have been published on the website. They show a balance sheet deficit of £784.4m including a pension scheme deficit of £921.1m which must be included under accounting rules. Were the pension scheme deficit to be excluded, net assets of £136.7m would be reported, representing a small increase of £0.3m over 2020-21.
- 5.2. Useable reserves were £35.8m as at 31 March 2022, a decrease of £9.9m since 2020-21. Reserves expenditure was on target with the plan for the year.
- 5.3. In order to determine and reach the conclusion that the Balance Sheet is robust specific areas of consideration were identified and reviewed, which were:
- Debts owed to the Authority;
  - Net worth of the Authority;
  - Adequacy of provisions held;
  - Reserves set aside – either earmarked or not and whether actually committed; and
  - The adequacy of the General Fund Balance to meet unforeseen expenditure.

### ***Cash Flow***

- 5.4. Financial Assets (excluding debtors) of the Authority were £35.2m as at 31 March 2022 (a decrease of £1.8m since 2020-21) and are held as a mixture of short and long term investments. Income from central government and billing authorities is received throughout the year which enables robust forecasting of cash flow.
- 5.5. Cash flow is reviewed by officers on a daily basis so any risks can be identified and mitigated. In 2021-22 there were no instances where the bank accounts were overdrawn and no short-term borrowing took place.
- 5.6. The Cash Flow forecast for the next 12 months has been reviewed. A continued healthy cash position is anticipated given the profile of income, revenue and reserves expenditure.

## **6. GOVERNANCE ARRANGEMENTS**

- 6.1. The Authority publishes, as part of its suite of year end reporting, an Annual Statement of Assurance. The Annual Statement of Assurance is reviewed taking account of external and internal audit reviews. Statements of assurance in the performance of internal controls and risk are sought from Service management. The effectiveness of the Authority's governance arrangements are reviewed annually together with the evidence to support it and then presented to this Committee. The last Annual Statement of Assurance (for the financial year 2021-22) was presented in draft form to this Committee at its meeting on 10 May 2022 (Minute \*AGC/21/22 refers).

- 6.2. Whilst it is not possible to secure absolute assurance, the annual review of the statement and assurance reports received during the year offers evidence that arrangements are fit for purpose and effective.

## **7. THE REGULATORY AND CONTROL ENVIRONMENT**

- 7.1. The Authority is required to operate within a highly legislated and controlled environment and particular emphasis of this can be exemplified and demonstrated with the financial controls in place. Examples of controls include the requirement of the Full Authority to approve a balanced annual budget, but within that to consider and have regard via assurance from the Treasurer as to the robustness of the budget, its estimates and the adequacy of reserves held.

- 7.2. The control environment is supported by the role of External Audit in auditing of the financial statements, the review of value for money and financial resilience. Further detail on the control environment of the Authority is available in the draft Annual Statement of Assurance as reported to the last meeting of this Committee.

- 7.3. The Service is also subject to a new inspection regime by Her Majesty's Inspectorate of Constabulary, Fire and Rescue Services (HMICFRS). The latest inspection was undertaken during quarter 2, 2021. The inspection report is due to be published soon. It will make reference to the performance of the Service in three areas: Effectiveness, Efficiency and People. The resulting improvement plan will be incorporated into the Authority's performance management reporting.

## **8. CONCLUSION**

- 8.1. The Authority operates within a robust control environment which can be evidenced by reviews of its assurance arrangements such as External and Internal Audit processes, neither of which have identified any significant issues in the past year.
- 8.2. In addition to backwards looking assurance, financial and operational monitoring processes are in place to mitigate risks within the financial year and are regularly reported to management and those charged with governance.
- 8.3. While inflation is causing some concern at present, the review of the financial indicators contained within this report together with planning assumptions for the Medium Term Financial Plan, Cash Flow and Reserves Strategy mean that there is a high level of confidence that the Authority will be able to continue as a going concern for the foreseeable future.

**Shayne Scott**  
**Director of Finance, People & Estates**  
**(Treasurer)**