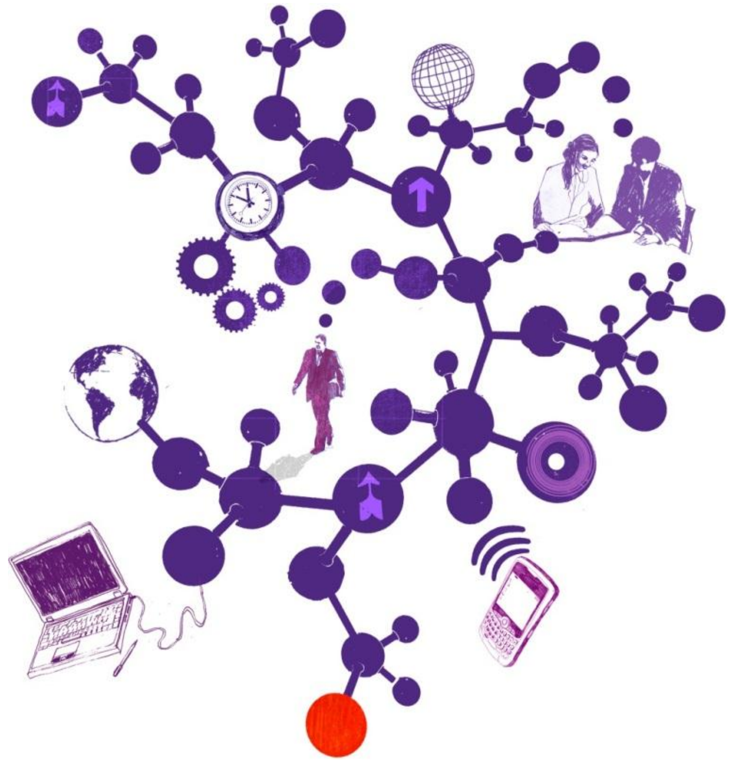
Review of the Council's Arrangements for Securing Financial Resilience for Kent County Council

Year ended 31 March 2013

5 July 2013



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Our approach

Value for Money Conclusion

Our work supporting our Value for Money (VfM) conclusion, as part of the statutory external audit, includes a review to determine if the Council has proper arrangements in place for securing financial resilience.

In so doing we have considered whether the Council has robust financial systems and processes in place to manage its financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future. We have carried out our work in discussion and agreement with officers and completed it in such a way as to minimise disruption to them.

The definition of foreseeable future for the purposes of this financial resilience review is 12 months from the date of this report.

We have reviewed the financial resilience of the Council by looking at:

- Key indicators of financial performance;
- Its approach to strategic financial planning;
- Its approach to financial governance; and
- Its approach to financial control.

Further detail on each of these areas is provided in the sections of the report that follow. Our overall conclusion is that the Council has put sound arrangements in place and adequately approached financial planning, governance and control. The primary scope of our work was the delivery of budgets during 2012/13, the financial planning for 2013/14 and the medium term plan. This report needs to be read in the context that 2012/13 is the second year of the four-year SR10 period, where some of the potential risks and challenges over the medium term may have yet to materialise.

We have used a red/amber/green (RAG) rating with the following definitions.

Green	**Arrangements meet or exceed adequate standards**. Adequate arrangements identified and key characteristics of good practice appear to be in place.
Amber	**Potential risks and/or weaknesses**. Adequate arrangements and characteristics are in place in some respects, but not all. Evidence that the Council is taking forward areas where arrangements need to be strengthened.
Red	**High risk**: The Council's arrangements are generally inadequate or may have a high risk of not succeeding

Executive Summary

National and Local Context

National Context

The Chancellor of the Exchequer announced the current Spending Review (SR10) to Parliament on 20 October 2010. SR10 represented the largest reductions in public spending since the 1920s. Revenue funding to local government was to reduce by 19% by 2014-15 (excluding schools, fire and police). After allowing for inflation, this equates to a 28% reduction in real terms with local government facing some of the largest cuts in the public sector. In addition, local government funding reductions were frontloaded, with 8% cash reductions in 2011-12. This followed a period of sustained growth in local government spending, which increased by 45% during the period 1997 to 2007.

The Chancellor of the Exchequer, in his Autumn Statement in November 2011, announced further public spending reductions of 0.9% in real terms in both 2015-16 and 2016-17. In his Autumn Statement on 5 December 2012, the Chancellor reinforced austerity measures announcing a further £6.6bn of savings during 2013-14 and 2014-15. Whilst health and schools will be continue to be protected in line with the Government's policy set out in SR10, local government will continue to face significant funding reductions. The Department for Communities and Local Government will contribute £470m of these additional savings, £445m of which will come from local authority funding during 2014-15, with local authorities being exempt from additional savings in 2013-14. In his March 2013 Budget the Chancellor announced further departmental 1% savings during each of 2013-14 and 2014-15. The NHS and schools remain protected, but police and local government will need to find an additional 0.5% over both years.

The next spending round period, 2015-16, was announced by the Chancellor on 26 June 2013. Local government will face a further 10% funding reduction for this period.

Local Context

Kent is divided into 12 local authority districts and Medway Unitary Authority. The Kent County Council (KCC) area excludes Medway. It is the largest County Council in the country. Kent's population is currently estimated to be 1,480,200 people with a forecast growing trend which is putting increasing pressure from higher demand on services.

Kent has traditionally been a high performing Council. In 2010 there was a 'poor' Ofsted inspection but the Council has worked hard since to improve the quality of the service and achieved an overall 'adequate' rating for children's services in January 2013.

Similar to all other public sector bodies, Kent is facing a significant financial challenge to deliver its current level of services with reducing funding. The Council is aware that it is one of the most challenging financial periods which means new ways of working need to be identified. The Council has made savings totalling £174 million in the past two years and has built in £95 million savings into the 2013/14 budget. The Council expects that it will have to make savings of a similar magnitude over the next three years.

The Chancellor's Autumn Statement announced a further reduction of 2% for local government in 2014/15 which added to previous announcements is likely to mean a reduction of £32.4m funding for KCC. The Council's current approach for setting the budget is to continue to avoid direct cuts to services wherever possible. It plans to use transformational change to deliver savings whilst continuing to provide a quality service with the reduced funding available.

Executive Summary

Overview of Arrangements

Risk area	Summary observations	High level risk assessment
Key Indicators of Performance	• We have reviewed six key indicators of performance using published financial ratios from the Audit Commission and benchmarking against the Council's nearest neighbour group. The review considered the following: liquidity; borrowing; workforce; performance against budgets; reserve balances; and schools balances. • Overall the ratio analysis has shown a relatively positive outlook for the Council with workforce, performance against budget and reserves improving over the past few years. • The Council's liquidity ratio is below the acceptable level of current assets to liabilities at 2:1 as the last published data (2011/12) shows a ratio of 1.22. The Council's ratio has been improving over the past couple of years and as at 31 March 2013 the liquidity is a ratio of 1.76. • Although the Council is an outlier for long term borrowing, the levels of debt are in line with its prudential indicators and treasury management policy.	Green
Strategic Financial Planning	• The Council has robust strategic financial planning arrangements in place. The Council's Medium Term Financial Plan is set for the period 2013-15 and takes account of the directorate and service business plans for the 2013/14 year. There are strong links between the MTFP and the Council's key priorities. • There was an extensive consultation of the 2013/14 budget over the summer of 2012. The Council used an external agency to undertake two full days of consultation with the public and Cabinet has analysed the results and published a formal response setting out its considerations and impact on the final budget. • The Council uses scenario planning in preparing its budget to understand the potential impact of decisions.	Green

Executive Summary

Overview of Arrangements

Risk area	Summary observations	High level risk assessment
Financial Governance	• The Council has sound financial governance arrangements. There is a robust process for setting the budget and identifying significant savings for the past two years. • Cabinet members are engaged and have an understanding of the financial environment the Council operates in. Training is to be provided for new members of the Governance & Audit Committee to ensure they understand the financial accounting environment before approving the 2012/13 financial statements. • The Council has limited understanding of its costs outside of the demand led services. Unit cost information for adults and children's services are reported quarterly to Cabinet, with a small number of other costs, but there is more the Council could do, especially as the financial environment becomes more challenging. • Financial health indicators are reported as part of the detailed quarterly revenue and capital budget monitoring to Cabinet. However, these indicators generally report the financial position at the end of the month being reported and are not forward looking into the medium or longer term.	Green
Financial Control	• The Council has well established financial control arrangements in place. Savings totalling £174m have been made in 2011/12 and 2012/13 with a further £95m identified in the 2013/14 budget. • The Council has effective finance and internal audit teams which are well placed to help the Council move forward in the difficult financial environment. • The risk management arrangements are improving although the Council has recognised that further improvements are required to embed the arrangements.	Green

Executive Summary

Next Steps

Area of review	Key points for consideration	Responsibility	Timescale	Management response
Key Indicators of Performance	The level of borrowing should continue to be monitored carefully to ensure continued affordability.	Corporate Board	Immediate	We have already set an upper limit of 15% of net revenue being used for debt repayment. This will be closely monitored on the rolling three year capital programme in development to ensure this limit is not breached.
Strategic Financial Planning	The Council should consider financial planning for the longer term by extending the MTFP over a 3-5 year period.	Corporate Director of Finance & Procurement	Immediate	We will consider MTFP term, including aligning with spending review periods and/or local election periods. We will introduce three year horizon planning as a minimum.
Financial Governance	The Council should improve awareness and understanding of key unit costs to aid decision making.	Corporate Director of Finance & Procurement	By November 2013	Training and information will be much more easily accessible.
Financial Control	The Council should continue to improve its risk management arrangements through effective use by all relevant staff of its new risk reporting system, GRACE.	Corporate Risk Manager	TBC	TBC

Key Indicators

Introduction

This section of the report includes analysis of key indicators of financial performance, benchmarked where this data is available. These indicators include:

- Working capital ratio
- Long term borrowing to tax revenue
- Long term borrowing to long term assets
- Sickness absence levels
- Out-turn against budget
- Useable Reserves: Gross Revenue Expenditure
- Schools Reserves - Balances to DSG allocations

Benchmark comparisons against KCC's nearest neighbours have been provided to officers as a separate appendix.

We have used the Audit Commission's nearest neighbours benchmarking group comprising the following County Councils:

Cambridgeshire
Derbyshire
Essex
Gloucestershire
Hampshire
Hertfordshire
Lancashire
Leicestershire
Northamptonshire
Nottinghamshire
Oxfordshire
Staffordshire
Warwickshire
West Sussex
Worcestershire

Key Indicators

Overview of performance

Area of focus	Summary observations	Assessment
Council's own financial health indicators	• The Council monitors its own performance against four financial health indicators; cash balances; long term debt maturity; outstanding debt owed to the Council and the percentage of payments made within payment terms. • The overall downward trend of cash balances held Since September 2009 reflects a policy to use cash to fund capital expenditure rather than borrow. The Council repaid £77m debt principal in 2012/13. Over the next four years, some £91m principal matures. Debt owed to the Council reduced by some £4m between March 2012 and Marc 2013, to a year end total of £19.4m. The Council paid 88% of payments within 30 days this year compared with 89% in 2011/12.	Green
Liquidity	• The working capital ratio indicates whether a council has enough current assets to cover its immediate liabilities. KCC's working capital ratio has been relatively stable in the range of 1.00 in 2008/09 to 1.22 in 2011/12. Comparative information on liquidity from the Council's statistical nearest neighbours shows its performance is within the 'norm'. The Council has calculated its liquidity as at 31 March 2013 and reported a ratio of 1.76 to Corporate Board.	Green
Borrowing	• The Council reports performance against prudential borrowing indicators in the full quarterly revenue and capital monitoring report in appendix 6. Its prudential borrowing indicator for 2012/13 was £1,154m. The operational boundary borrowing position (excluding Medway Council debt) as at 31 March 2013 is £969m which means the indicator has been met. • The Council set an authorised limit for external debt of £1,195m for 2012/13. It has not needed to utilise the additional borrowing limits in the financial year. • The Council's Long-term Borrowing to Council Tax Revenue is 1.92 which indicates that it has long term borrowing which exceeds tax revenue by almost two times. This is the highest amongst the comparator group, with other authorities typically having a ratio of 1 or less. The Council's ratio of long-term borrowing to long-term assets is 0.54 in 2011/12. This compares to the median of the comparator group of 0.3. In recognition of its comparative long term borrowing ratio the Council has set a prudential indicator of 15% of net revenue being used for debt repayment.	Green
Workforce	• The average sickness absence level for the public sector in 2011-2 was 7.9 days per FTE, local government average was 8.0 and the private sector average for the same year was 5.7. Many councils have taken a proactive approach to reducing the number of days lost to sickness each year as it often results in additional costs through using agency staff. • In comparison, the Council's performance was 7.8 days. In 2012/13, this reduced to a weighted average of 7.5 days. • The Council reports sickness absence targets in the quarterly performance report presented to Cabinet. The quarterly results for 2012/13 are: June 2012 - 7.7; Sep 12 – 7.5; Dec 12 – 7.3; and Mar 13 – 7.4. The Council is in line with the trend of falling sickness absence levels in the public and private sector.	Green

Key Indicators

Overview of performance

Area of focus	Summary observations	Assessment
Performance Against Budgets: revenue & capital	• The Council has achieved an underspend for the past 13 years. • The year end financial outturn shows an underspend of £16.081m (excluding schools). This is offset by a reported reduction in school reserves for 2012/13 of £10.964m. This gives a total underspend as at 31 march 2013 of £5.117m. • The year end capital outturn is also an underspend with £41m capital money being re-phased into the 2013/14 financial year.	Green
Reserve Balances	• The Council has maintained the level of general fund reserve, in line with its MTFP 2013-15, at £31.7m at year end. This amounts to 3.3% of the 2013/14 net revenue budget, and 2.2% of the gross revenue budget (excluding schools). The movement of +£22.4m in earmarked reserves in 2012/13 is clearly identified in the 2012/13 financial statements and explained in the outturn report being presented to Cabinet on 15 July 2013. • The useable reserves to gross revenue expenditure ratio is around 14% for 2011/12 and has increased to around 18% for 2012/13. There has been a relatively steady position for reserve balances over the past five years. Compared with its comparator group, KCC is below the median.	Green
Schools Balances	• The 2012/13 accounts showed a total carry forward to 2013/14 of £16,488k. This represents a carry forward of £10,274k on the centrally retained DSG budget and £6,606k on the schools' unallocated budget. The schools unallocated reserve now stands at over £9m, and its use is determined by the Schools' Funding Forum who have committed the majority of the unallocated reserve and estimated that over half will be spent in 2013/14. • The Council's share of schools balances in relation to the total DSG allocation received for the year is 7%. This is at the average for the peer group. • The Council's schools have been reducing their balances and the Council should continue to monitor this to ensure balances remain at a reasonable level. Some of the reduction in balances is linked to the removal of balances held by schools who have transferred to academy status in the year.	Green

Strategic Financial Planning

Key characteristics of good strategic financial planning

In conducting our review of strategic financial planning we have assessed the Council's performance against the following indicators:

- Focus on achievement of corporate priorities is evident through the financial planning process. The MTFP focuses resources on priorities.
- The MTFP includes outcome measures, scenario planning, benchmarking, resource planning and details on partnership working. Targets have been set for future periods in respect of reserve balances, prudential indicators etc.
- Annual financial plans follow the longer term financial strategy.
- There is regular review of the MTFP and the assumptions made within it. The Council responds to changing circumstances and manages its financial risks.
- The Council has performed stress testing on its model using a range of economic assumptions including CSR.
- The MTFP is linked to and is consistent with other key strategies, including workforce.
- KPIs can be derived for future periods from the information included within the MTFP.

Strategic Financial Planning

Medium Term Financial Strategy

<table>
<tr><th>Area of focus</th><th>Summary observations</th><th>Assessment</th></tr>
<tr><td>Focus of the MTFP</td><td>

The Council has developed a Medium Term Financial Plan (MTFP) for 2013-2015. This was approved by the County Council alongside the revenue and capital budgets for 2013/14 on 14 February 2013. The Council has balanced its budget for 2013/14, identifying revenue savings of £95 million. The MTFP includes the national and local context for Kent to establish the overall challenges the Council is facing. For 2013/14, this is a reduction of around £39 million in government grants (equates to 9.5%). This is estimated to be 4% of net spending.
The MTFP includes clear spending demands and pressures alongside the potential income generation and savings proposals. As part of the budget proposals the Council has confirmed that it will continue to use the Council's cash reserves to protect front-line services. However, is has recognised that reserves will need to be replaced if consumed and this is not a long term solution to a budget deficit. For 2013/14, the Council has used £9m of earmarked reserves to balance the budget.
The budget strategy for 2013/14 and beyond, as set out in the MTFP, is based around the 4 P's:

Prevention: the Council plans to move away from expensive reactive service provision to investing in preventative models that are cost effective and deliver better outcomes. This is shown in the investment of the health money in adults transformation project.
Productivity: The Council has identified that it needs to deliver a step change in the productivity of its services and staff. It plans to do this through greater integration around its key client groups and by investing in back office support systems and procedures to release resources to the front line.
Procurement: the Council aims to introduce the best business and service practice found across the private sector for procuring its goods and services.
Partnership: the Council has identified that to make a reality of the above three areas it must have effective partnerships across all Kent public services so the benefit is seen across the county. This is required for joint commissioning and service delivery.

The Vision for Kent is the Council's countywide strategy for the social, economic and environmental wellbeing of Kent's communities. This sets out a 10-year vision for these ambitions with the capital investment programme focussed on achieving the vision. The capital programme is set for the period 2013-2016. The Council set a new capital strategy for 2013/14 which focuses on capital investment and a greater focus on the Council's strategic priorities to ensure it maximises the value of its assets. It has developed fiscal indicators in the strategy with the key indicator being to limit the cost of borrowing to 15% of overall revenue and capital spend. The capital programme shows an investment of £695m over three years from 2013/14, with £107.8m funded from borrowing.

</td><td>Green</td></tr>
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Strategic Financial Planning (continued)

Area of focus	Summary observations	Assessment
Adequacy of planning assumptions	• The assumptions around the national budget announcements and pressures are built into the MTFP, with the Council providing a clear assessment of how it is has interpreted this in relation to the residents of Kent. For example, due to the continued pressures on household income across Kent, particularly with the introduction of the welfare reform changes to some of the poorest families in the county, the Council has frozen council tax for the third consecutive year in 2013/14. • Arrangements for effective future financial planning are sound. The Council decided to develop three year service strategies for all directorates from 2012/13 to assist in the transformation of the Council's services against a backdrop of long-term financial decline. These strategies were to be shaped around: vision and innovation; risks and implications; and helping to shape the future. The Budget Programme Board has continued its work during the 2012/13 financial year and has challenged Directors and Heads of Service where strategies are not realistic to ensure that planning assumptions built into the service plans can be relied upon. This process is on-going and the Council has realised the importance of the BPB's work. • The 2013/14 budget process built in scenario planning and stress testing over the summer of 2012. The timing of the process ensured that there was sufficient learning from the public consultation. The medium to long term assumptions appear reasonable for the future financial position. The Council remains prudent in its spending plans and recognises that savings will be more difficult to achieve in the future without cutting services. • The Council does not routinely benchmark itself against other local authorities. It used to take part in the CIPFA benchmarking club but data was not sufficiently up to date to be beneficial to the decision making process or understanding of its budget base so it stopped participating two years ago.	Green
Scope of the MTFP and links to annual planning	• The Council's MTFP 13-15 is linked closely with the Bold Steps for Kent and other key Council policies. The budget is linked to the individual Business Plans for 2013/14 submitted by directorates for Cabinet approval in April 2013. This built on the business plans developed for 2012/13 with an enhanced focus on cross cutting plans between directorates/services and early engagement of Cabinet Committees in shaping headline priorities and pre-scrutiny of early draft plans . The business planning process has helped divisions plan ahead earlier for future capacity and demands which focuses them on the financial challenges they face. • The Council used an external agency to undertake two consultation days with local people and partners in east and west Kent as part of budget setting process for 2013/14. The approach involved high level consultation on the broad shape and objectives of the budget and services the Council can provide with the reduced funding allocation. The consultation has focussed the Council's priorities as well as identifying areas of the budget that the public believe should be protected.	Green

Strategic Financial Planning (continued)

Area of focus	Summary observations	Assessment
Review processes	• The MTFP is reviewed and updated as part of the annual planning cycle. The Council has identified that the plan only gives a forward view for two years but believes a longer term plan is not possible given the uncertainties around funding from government. This is reasonable as there is not sufficient information available for the Council to use to realistically predict the budget for 15/16 and beyond. • The Council reviews its financial performance regularly with quarterly reporting to Cabinet on the Council's achievement of its corporate priorities. The reporting is clear and focused on the risk areas and performance targets that are not being met.	Green
Responsiveness of the Plan	• The Council published an early draft consultation of the budget in the summer of 2012. 416 members of the public, in addition to the specific consultation with stakeholder groups, commented on the draft budget proposals. Cabinet formally considered the responses received from the consultation at its meeting in December 2012 and this informed the next version of the draft MTFP. • Due to the late announcement of the provisional local government finance settlement the revised final draft budget could not be published until January which is later than originally intended as it only gave a short window for further consultation. This consultation required £14.8 million more savings than in the first draft due to the final budget announcement. The MTFP had sufficient flexibility to enable members to respond to these further pressures by identifying savings to ensure that the budget presented for County Council approval in February was balanced. • There remains significant uncertainty about the financial position for 2014/15 and beyond. The Council has a good track recording of delivering its annual budgets and savings plans which gives confidence that the business planning process is resilient enough to ensure that good outcomes can be maintained despite major spending reductions. • The Council undertakes scenario planning for its major areas of spend and uses this to inform decision making. Members and officers have a clear understanding and awareness of the challenges the Council faces and that new ways of working need to be developed.	Green

Financial Governance

Key characteristics of effective financial governance

In conducting our review of financial governance we have assessed the Council's performance against the following indicators:

Understanding

- There is a clear understanding of the financial environment the Council is operating within:
  - Regular reporting to Members. Reports include detail of action planning and variance analysis etc.
  - Actions have been taken to address key risk areas.
  - Officers and managers understand the financial implications of current and alternative policies, programmes and activities.

Engagement

- There is engagement with stakeholders including budget consultations.

Monitoring and review

- There are comprehensive policies and procedures in place for Members, Officers and budget holders which clearly outline responsibilities.
- Number of internal and external recommendations overdue for implementation.
- Committees and Cabinet regularly review performance and it is subject to appropriate levels of scrutiny.
- There are effective recovery plans in place (if required).

Financial Governance

Understanding and engagement

Area of focus	Summary observations	Assessment
Understanding the Financial Environment	• The Corporate Board has a sound understanding of the financial environment that the Council operates within. The introduction to the annual budget and MTFP sets out the national and local pressures and identifies the need for integrated thinking to meet these pressures, not only within the Council, but with its stakeholders. The Council is aware of the main risks that it faces and has set these out in the MTFP in the financial risks and opportunities section. The amounts reported are not included in the 2013/14 budget but have been identified as potential issues/opportunities for the Council to incorporate into the budget during the financial year. • The Council understands the financial challenges facing its stakeholders. It has continued to work with small and medium businesses in Kent and is an agent for the Regional Growth Fund money to help expand businesses in East Kent by creating / protecting jobs in an area of high unemployment. • The Cabinet receives quarterly revenue and capital budget monitoring reports which include detailed variance analysis and explanations on a directorate basis. The report also details the Council's key activity indicators and financial health indicators which gives decision makers the relevant information to make informed decisions. • Financial awareness training is provided to budget holders and a training session is being provided at the start of the Governance and Audit Committee in July 2013 to ensure that new members are aware of the financial environment and accounting framework before approving the 2012/13 financial statements. • The Council has approved and communicated to staff and members the financial instructions and standing orders in which the Council operates. These have been issued to all officers with financial management responsibilities. We have not identified any breaches in the Council's compliance with the financial regulations during 2012/13.	Green
Executive and Member Engagement	• There is strong member and corporate director engagement on financial matters through the Corporate Board. • Cabinet portfolio holders are actively engaged in the budget setting and monitoring financial delivery. Members are aware of the need for greater savings in future years, and that services will need to be provided differently if the Council is to meet the demand against the increasing pressures.	Green

Financial Governance (continued)

Understanding and engagement

Area of focus	Summary observations	Assessment
Executive and Member Engagement (continued)	• Members outside of Cabinet are also actively involved in understanding the financial environment in which the Council operates. The business planning process for 2013/14 was reviewed and challenged by Cabinet Committees. A report to Cabinet commented on the positive impact of Cabinet Committees' review and challenge of the business planning process. • The Governance and Audit Committee meet throughout the year and have clear terms of reference for their responsibilities in ensuring the financial governance of the Council. There is a member work and development programme that is reviewed at every committee meeting to ensure that the committee is carrying out its function. The Committee's membership has changed following the elections in May 2013 and the Council has training planned to ensure that new members are properly equipped to effectively carry out their role.	
Overview for controls over key cost categories	• The Council monitors and reports the revenue budget on a portfolio basis. The Council has been going through a major restructure since the start of 2011/12 and changed its portfolio and coding structure in the ledger in that financial year. The reporting from the ledger is based on the portfolios. • The resource allocations note in the 2012/13 financial statements has been prepared on the portfolio basis. The note does include the adults and specialist children's services as one 'families and social care directorate but this has been accepted as both services are the responsibility of one Corporate Director. • The Council has acknowledged that it does not understand all of its costs and that this is an area to be strengthened in the future. Currently, the reporting of budgets on a unit cost basis is focussed on the demand-led services of adults and children's social care. This is set out in appendix 4 of the quarterly budget monitoring report to Cabinet. • Financial regulations are reviewed and updated as appropriate.	Amber
Budget reporting: revenue and capital	• The Council reports the full revenue and capital budget position on a quarterly basis to Cabinet. The reports enable members to make informed decisions on the budgeted outturn position and for corporate directors to understand the financial position. These are very detailed reports, including explanations for all significant variances. The Council has identified that it needs to improve the budget monitoring reports to make them more accessible for members. The reports need to be more concise to give members a snapshot of the overall financial position and key risk areas.	Green

Financial Governance (continued)

Understanding and engagement

Area of focus	Summary observations	Assessment
Budget reporting: revenue and capital (continued)	• Budget monitoring exception reports are presented to Cabinet in the intervening months. These highlight significant issues arising in a specific budget since the last full quarterly report. These reports give the Cabinet sufficient information to make decisions as necessary in between the detailed reporting. • The quarterly budget reports set out the predicted revenue and capital budget outturns on a portfolio basis. Although the overall report is long, the level of variance analysis within the reports is considered appropriate to explain the variance. • Monthly budget reports for revenue and capital are produced for the budget holder. The management accountant linked to the service meets with the budget holder to discuss action needed for variances. The report level is sufficient to allow the budget holder to understand the budget and position for the month and year to date. • The year end financial outturn shows an underspend of £16.081m (excluding schools). This is offset by a reported reduction in school reserves for 2012/13 of £10.964m. This gives a total underspend as at 31 march 2013 of £5.117m. All portfolios were underspent with the exception of specialist children's services. The reasons for the overspend are widely reported. Much investment has been made to improve the service. This has been successful as evidenced by Ofsted's re-inspection report in January 2013 rating the service as 'adequate'. The challenge for the service is to continue the rate of improvement whilst meeting its budgeted outturn. • The year end outturn for the capital programme shows an underspend of £41.899m against the revised approved budget totalling £202.998m. This represents slippage of 21% in 2012/13. The main reasons for under-spending are operational delays and project slippage with £43.871m being re-phased into 2013/14. The net underspend position included £4.388m additional funded variances and £2.416m project underspends. The Council needs to ensure that the capital programmes is robustly planned and monitored to ensure slippage of this magnitude does not occur again.	Green
Adequacy of other Committee/ Cabinet Reporting	• The Cabinet meets every month. There is a clear agenda and forward plan for the meetings. It discusses and takes decisions on the most significant issues facing the Council. The quarterly budget reports include financial health indicators covering cash balances, debt, payments made within agreed terms and inflation indices. • The Council has established five Cabinet Committees from 1 April 2012 that meet throughout the year. The purpose of the committees is to consider the functions of the Council that are the responsibility of the related Cabinet Members. They review the key decisions and reports that are being presented to Cabinet which gives added governance focus to the issues. In addition, a new suite of Scrutiny Committees was established at the same time.	Green

Financial Control

Key characteristics of effective financial control

In conducting our review of financial control we have assessed the Council's performance against the following indicators:

Budget setting and budget monitoring

- Budgets are robust and prepared in a timely fashion.
- Budgets are monitored at an officer, member and Cabinet level and officers are held accountable for budgetary performance.
- Financial forecasting is well-developed and forecasts are subject to regular review.

Savings Plans

- Processes for identifying, delivering and monitoring savings plan schemes are robust, well thought through and effective.

Financial Systems

- Key financial systems have received satisfactory reports from internal and external audit.
- Financial systems are adequate for future needs.

Finance Department

- The capacity and capability of the Finance Department is fit for purpose.

Internal Control

- There is an effective internal audit which has the proper profile within the organisation. Agreed Internal Audit recommendations are routinely implemented in a timely manner.
- There is a an assurance framework in place which is used effectively by the Council and business risks are managed and controlled.

Financial Control

Internal arrangements

Area of focus	Summary observations	Assessment
Budget setting and monitoring - revenue and capital	• The Council has a robust process in place for setting the budget and has a strong record of achieving its budgeted outturn with an underspend for the past 13 years. There is a clear understanding of the financial pressures whilst meeting the priorities set out in the Bold Steps for Kent. • The Council met its aim to publish the 2013/14 budget much earlier than in previous years, with the draft budget published for consultation in the summer of 2012. This allowed for longer review of the draft budget by its stakeholders, and for members to give full consideration to the responses before approving the final budget in February 2013. The Cabinet's response to the consultation feedback is available on the Council's website. • The annual budget is built from a historical baseline adjusted for any growth, inflationary pressures and savings options. The Budget Book sets out the budget in an a-z alphabetical listing identifying individual service budgets and which portfolio is responsible for each line in the Budget. It also shows key performance and affordable activity levels. The services continue to be split into four main sections: Direct service to the public; Financing items; Assessment services; and Management, support services (including support to front line services) and overheads. • The Budget Book also sets out the revenue budget on a directorate basis for an overall view of the service area a Corporate Director is responsible for. • The Council has revised its three year capital programme forecast of £629.4m with a forecast underspend of £18.5m in the MTFP 2013-15. This is due to variances on a number of projects, as well as aligning some of the planned schemes in line with the new Capital Strategy.	Green
Performance against Savings Plans	• The Council has a robust process in place for identifying and monitoring savings. The savings target for 2012/13 was £79m which was achieved by year end. Of the revenue underspend of £16.081m, the Cabinet is being asked to approve the rolling forward of the uncommitted underspend of £4.9m into reserves pending future budget decisions as it is recognised that the savings pressures are becoming increasingly difficult to identify and there will continue to be significant government cuts over the medium term. Historically, the Council has a good track record of meeting its budget and delivering the required savings every year. • The savings target for the 2013-14 financial year is £95m. 2013/14 budget setting followed the same process as adopted in 2011/12 and budget savings to be identified within each directorate. An update report was presented to the Governance and Audit Committee in April 2013 setting out the BRAG ratings of each of the savings: £41m savings are already blue (banked); £18m were green; and £36m were amber.	

Financial Control

Internal arrangements

Area of focus	Summary observations	Assessment

Performance against Savings Plans (continued)	• We reviewed two of the amber rated savings plans as part of our financial resilience work to determine how realistic the savings targets were. We agreed the Council's RAG assessment for both:
	  • adults transformation £18.1m – we have reported this work in detail in the Audit Findings Report as part of the value for money conclusion. Overall, the Council does not yet have a clear understanding of how the £18.1m savings will be made in 2013/14. The Council's partner Newton Europe has undertaken initial work and identified for review, commissioning, care pathways and optimisation. A progress report is expected on 22 July. The Council anticipates that the detailed planning will deliver some financial savings in 2013/14, but acknowledges there is a risk over the quantum of £18m being delivered. It has a number of mitigating actions to address any shortfall.
	  • workforce terms and conditions (T&Cs) review and reduction of 100 non-frontline posts £2.3m – Of the £2.3m savings to be made in 2013/14, about £1.3m is to be realised from the terms and conditions review, with £800k already identified as savings by each directorate. HR presented a paper for the proposed changes to T&Cs to the Personnel Committee in January 2013. Following this paper, HR has carried out a 'floor walking' exercise to understand how staff are affected by the proposed changes. The outcome of this is due to be reported to CMT in July. A decision on how to achieve the balance of £500k savings will also need to be made.
	• All savings identified in the budget are owned by Heads of Service. For all projects over £200,000 the responsible directorate/ manager prepares a Project Initiation Document (PID) identifying how savings will be delivered, the quantum of savings and project milestones. A formal review of the 2012/13 PIDs was carried out in September 2012 to ensure the proper rating had been assigned by the responsible officer halfway through the year. This helped the Council to meet the overall savings target for 2012/13. The focus for monitoring and review of the overall budget continues with the usual budget monitoring process.
	• The Council established the Budget Programme Board (BPB), a mixed group of members and officers, in October 2011. The Cabinet Member for Finance chairs the weekly meetings. The initial focus of the BPB was to monitor the budget and hold budget holders to account for their PIDs which support the detailed savings plans. The Council has continued the BPB as this group has helped to drive the required efficiencies and ensure that savings are realised as planned at the directorate level. However, due to the successes of the PID process in 2012/13, the Council evolved the process for 2013/14 to give the Heads of Service (as responsible owners) greater individual monitoring responsibility. Only high risk PIDs were collated centrally and reported to the BPB. The Council has identified that this is not as effective as the process in 2012/13 and is going to ask for all PIDs to be submitted centrally for 2014/15. This is important in the increasingly difficult financial environment.
		Amber

Financial Control

Internal and external assurances

Area of focus	Summary observations	Assessment
Performance against Savings Plans (continued)	• The PIDs will be electronically linked to the MTFP from 2014/15. • The Council has maintained the level of general fund reserve, in line with its MTFP 2013-15, at £31.7m at year end. This amounts to 3.3% of the 2013/14 net revenue budget, and 2.2% of the gross revenue budget (excluding schools). The movement of +£22.4m in earmarked reserves in 2012/13 is clearly identified in the 2012/13 financial statements and explained in the outturn report being presented to Cabinet on 15 July 2013.	
Key Financial Accounting Systems	• The Council has used Oracle as its main accounting system for a number of years which it has developed internally using the skills of its in-house ICT department to meet its financial monitoring and reporting needs. • There is a sound understanding of the ledger within the financial systems team. They are able to interrogate the system and run specialist reports as needed by budget holders and directors. • The Council has a strong history of producing its accounts earlier than the statutory 30 June deadline to receive its audit opinion towards the end of July. It is the earliest county council to receive an audit opinion which is a result of the liaison and co-operation with its external auditors. • Internal Audit has not reported any limited assurance reports on the key financial systems during 2012/13.	Green
Finance Department Resourcing	• The Council has undergone a significant restructuring over the past two years. The finance department restructure was in early 2012/13 financial year. This centralised the finance staff from the previous devolved directorate finance teams. Although there has been a reduction in the number of finance staff overall at the Council the finance team has sufficient capacity to carry out its function effectively. • The Corporate Director of Finance and Procurement is well respected across the Council and is a member of Corporate Management Team so has a good oversight of the financial impact of all key decisions made. • The Chief Accountant and Capital Finance Managers were new in their posts at the start of the financial year. The accounts were produced in line with the Council's early closedown deadline and the audit has been completed in the short audit visit which confirms the competency and knowledge of the finance team.	Green

Financial Control

Internal and external assurances

Area of focus	Summary observations	Assessment
Internal audit arrangements	• The Internal Audit department has undergone a number of changes in the year and has sufficient staffing to deliver the work programme for 2012/13. To enhance capacity of the team, the Council is using experienced contract staff for some of the reactive investigation work as well as more detailed projects, and Deloittes for the IT audit programme. The team has undertaken two investigations on behalf of Grant Thornton following concerns by members of the public. • As at the end of February 2013 the Internal Audit Plan for 2012/13 was 85% complete which is ahead of target. The Head of Internal Audit is confident that the targeted completion of 90% will be exceeded by year end. This will be reported to the July Governance and Audit Committee (G&AC). • Internal Audit has raised its profile within the Council over the past year and is experiencing a greater workload as officers in the directorates request investigations or audits. A summary of all work completed is reported to the G&AC with follow up of the recommendations made as a standard part of the progress report. • The Internal Audit team has reviewed the Public Sector Internal Auditing Standards which came into effect on 1 April 2013. There are no fundamental differences between the new standards and previous standards included in the CIPFA Code of Practice. The Council will need to obtain external verification of their compliance with the standards.	Green
Assurance framework/risk management	• Due to weaknesses identified by Internal Audit and the previous external auditor, we undertook a review of the risk management arrangements in 2012/13 as part of the VFM conclusion and reported our findings in the Audit Findings Report. This review placed reliance on the work of Internal Audit's follow up review in year. Internal Audit's report was issued in June 2013 with an overall assurance rating of 'adequate'. • The Corporate Risk Manager has been in post for a year which has led to improvements in the arrangements. However, there is still more work to be done to embed the risk register arrangements, including the use of the new system GRACE, across the Council. There remains inconsistencies between directorates/divisional registers and the monitoring of risk.	Amber

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