

## ASSESSMENT OF GOING CONCERN

Portfolio	Finance
Ward(s) Affected:	n/a

### **Purpose**

This report informs the Committee of the S151 Officer's (Executive Head of Finance) assessment of the Council as a "going concern" for the purposes of producing the Statement of Accounts for 2016/17.

## **1. Background**

### **Key Issues: Assessment**

- 1.1 The concept of a 'going concern' assumes that an authority, its functions and services will continue in operational existence for the foreseeable future. This assumption underpins the accounts drawn up under the Local Authority Code of Accounting Practice and is made because local authorities carry out functions essential to the local community and are themselves revenue-raising bodies (with limits on their revenue-raising powers arising only at the discretion of central government). If an authority were in financial difficulty, the prospects are thus that alternative arrangements might be made by central government either for the continuation of the services it provides or for assistance with the recovery of a deficit over more than one financial year.
- 1.2 Where the 'going concern' concept is not the case, particular care would be needed in the valuation of assets, as inventories and property, plant and equipment may not be realisable at their book values and provisions may be needed for closure costs or redundancies. An inability to apply the going concern concept would potentially have a fundamental impact on the financial statements. Given the significant reduction in funding for local government in recent years and the potential threat this poses to the ongoing viability of one or more councils as a consequence, External Auditors are placing a greater emphasis on local authorities undertaking an assessment of the 'going concern' basis on which they prepare their financial statements. In response this report sets out the position at Surrey Heath.
- 1.3 As with all principal local authorities, the Council is required to compile its Statement of Accounts in accordance with the Code of Practice on Local Authority Accounting for 2016/17 (hereafter referred to as the Code) as published by the Chartered Institute of Public Finance and Accountancy (CIPFA). In accordance with the Code the Council's Statement of Accounts is prepared assuming that the Council will continue to operate in the foreseeable future and that it is able to do so within the current and anticipated resources available. By this, it is meant that the Council will realise its assets and settle its obligations in the normal course of business. The main factors which underpin this assessment are:
  - The Council's current financial position;
  - The Council's projected financial position;
  - The Council's strategic planning and budget framework process;
  - The regulatory and control environment applicable to the Council as a local authority;

### **The Council's Current Financial Position**

- 1.4 Overall the Council has ended the year under budget. Additional income has been earned from assets purchased in the year which was not budgeted for and there have also been savings in a number of areas.
- 1.5 Capital schemes have also come in in on or under budget and all expenditure has been funded. At the 31<sup>st</sup> March 2017 the Council had net borrowings of £119m against a Capital Funding Requirement (CFR) of £140m meaning that the Council is funding £21m of capital expenditure internally which could in an emergency be converted in to external debt. This would be within the current authorised limit of £167m.

### **The Council's Projected Financial Position (Revenue)**

- 1.6 The Council set a balanced budget for 2017/18 as required by law in February 2017. For the first time for a number of years no savings target was included and the Council did not have to use any "New Homes Bonus" to support expenditure. This was because of the significant investments in property made in the preceding year which have contributed £1.5m to revenue budget as additional income after financing and capital repayments. The Council has adopted a strategy of increasing income rather than cutting services, as outlined in the Medium Term Financial Plan, and this is being generated by property investment. The result of the investments made so far is to reduce the projected shortfall in resources in the budget for 2020/21 from £1.4m projected in 2016/17 to £222k projected in 2017/18.
- 1.7 The Council intends to make further investments during the year to try to insulate its finances and hence protect services from the uncertainty in Government funding from new homes bonus and business rates.
- 1.8 There are risks around property ownership but the Council is investing in a mixed portfolio of properties with a large number of tenants rather than being dependent on one key property and tenant. If in the next 12 months 25% of the Council's property portfolio was to become vacant this would result in an income loss of £1.6m. This could in the short term be covered by reserves thereby giving the Council time to change its property strategy and rebuild its income. This in term may require further borrowing or assets to be sold.

### **The Council's Current and Projected Financial Position (Capital)**

- 1.9. The Council set a capital budget of £3.8m for 2017/18 of which £3.2m related to the purchase of vehicles to support the new waste contract. This will be repaid over the next 10 years. The Council does not have any capital receipts and so any capital program has to be funded by loans or grant with the remainder coming from revenue. Only £21k of the capital program is forecast to be funded from revenue during the year and can be covered by reserves if required. It is likely that the Council will purchase further property during the year supported by borrowing but this will only be undertaken if it complies with the property investment policy and therefore can cover its own borrowing costs and capital repayments.

### **The Council's Balance sheet as at the 31<sup>st</sup> March 2017**

- 1.10. The unaudited financial statements show that the Council has a net balance sheet of £40m at the 31<sup>st</sup> March 2017 compared with £48m last year. Although the council has invested £120m in property this year this has all been funded by borrowing and so has not had an impact on the balance sheet. Most of the variance £8.5m is due to a change in the IAS19 pension liability driven by the continuing low Gilt rates used to value future obligations. However the triennial actuarial review as at the 31<sup>st</sup> March 2016 calculated the deficit to be £15m with a funding rate of 81% - a significant improvement on 2013. This meant that the actuaries did not need to recommend an increase in contributions as they believe that the fund is sustainable at the current rate of funding so there is no cause for concern about the increase in the pension liability.
- 1.11. The Council's balance sheet is underpinned with £200m in assets some of which could be sold if required. The Council also has cash backed reserves of £20m which could also be called upon.

### **The Council's Cash Flow**

- 1.12. The Council maintains a cash flow projection covering the whole financial year. This is so that borrowings and investment can be managed to ensure that there are adequate funds available to meet the Council's commitments. The Council held £10m in investments at the 31<sup>st</sup> March 2017 which could be converted into cash if required and in addition the Council could borrow on demand £20m from the Public Works Loans Board to meet its Capital Funding Requirement Gap to provide additional liquidity. On a day to day basis the Council can also access funds from the bank for short periods in the form of an overdraft or borrow from other local authorities provided that that overall debt ceiling is not breached.

### **The Council's Governance Arrangements**

- 1.13. The Council has a well-established and robust corporate governance framework. This includes the statutory elements like the post of Head of Paid Service, the Monitoring Officer and the Section 151 Officer in addition to the current political arrangements.
- 1.14. An overview of this governance framework is provided within the Annual Governance Statement which is included elsewhere on this agenda. This includes a detailed review of the effectiveness of the council's governance arrangements. Whilst it is not possible to provide absolute assurance the review process as outlined in the Annual Governance Statement does conclude that the existing arrangements remain fit for purposes and help provide assurance of their effectiveness.

### **The External Regulatory and Control Environment**

- 1.15. As a local authority the Council has to operate within a highly legislated and controlled environment. An example of this is the requirement for a balanced budget each year combined with the legal requirement for council to have regard to consideration of such matters as the robustness of budget estimates and the adequacy of reserves. In addition to the legal framework and central government control there are other factors such as the role undertaken by External Audit as well as the statutory requirement in some cases for compliance with best practice and guidance published by CIPFA and other relevant bodies.

- 1.16. Against this backdrop it is considered unlikely that a local authority would be 'allowed to fail' with the likelihood being, when faced with such a scenario, that central government would intervene supported by organisations such as the Local Government Association to bring about the required improvements or help maintain service delivery.

## **2. Conclusions**

- 2.1. It is considered that having regard to the Council's arrangements and such factors as highlighted in this report that the Council remains a "going concern". This assessment will be undertaken annually in the course of preparing the Council's financial statements for each year.

## **3. Options**

- 3.1 There are no options as the committee is asked to note and comment on the report.

## **4. Legal Issues**

- 4.1 The Council is required to compile its Statement of Accounts in accordance with the Code of Practice on Local Authority Accounting for 2015/16 (hereafter referred to as the Code) as published by the Chartered Institute of Public Finance and Accountancy (CIPFA). In accordance with the Code the council's Statement of Accounts is prepared assuming that the council will continue to operate in the foreseeable future and that it is able to do so within the current and anticipated resources available. By this, it is meant that the council will realise its assets and settle its obligations in the normal course of business.
- 4.2 This report sets out the process that has been undertaken in order to ensure that the Council complies with the relevant requirements of the Code and that it is "going concern" for the purposes of the draft statement of accounts 2016/17.

## **5. Governance Issues**

- 5.1 None

## **6. Sustainability**

- 6.1 The Council needs to be financially sustainable if services are to be maintained

## **7. Risk Management**

- 7.1 The Council has sought to mitigate risks to its finances as much as possible by ensuring that a balanced budget is set and adhered to, adequate levels of reserves are held and seeking to generate income. The main risk the council, and all public bodies face, is the uncertainty in respect of funding from central government and indeed the movement to charge a "fee" to some Councils thereby transferring money to Government. Surrey Heath has attempted to reduce this list by developing other forms of funding. Members are advised of potential changes in Government funding and the impact it could have in the Medium Term Financial Forecast, the annual budget and on an ad hoc basis when consultation responses are required.

## 8. Recommendation

- 8.1 The Audit Committee is recommended to note the outcome of the assessment made of the Council's status as a "going concern" for the purposes of the draft Statement of Accounts for 2016/17.

## 9. Resource Implications

- 9.1 There are no direct resource implications arising from this report however were the Council not considered to be a "going concern" this would have significant financial and governance implications as well as an impact on services

<b>Annexes</b>	<b>None</b>
<b>Background Papers</b>	<b>None</b>
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