

Towards a tipping point?

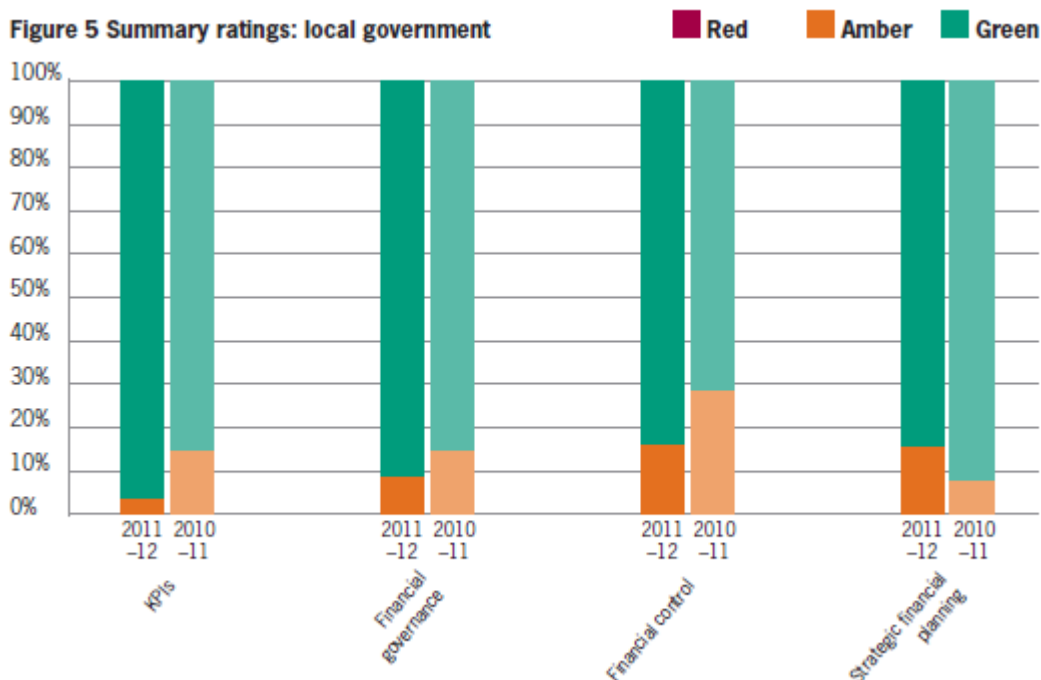
**Summary findings from our second year of financial health checks of English local authorities**

Report by Grant Thornton (December 2012)

**Summary and conclusions**

*Overall, local authorities have continued to manage in the current environment, but improving scenario planning, sensitivity analysis and reporting of savings programmes as well as ensuring financial governance arrangements remain robust will help finance management to influence key stakeholders in the uncertain times ahead.*

The overall trend for many of the categories we have rated is a slightly improving position between 2010–11 and 2011–12. This is replicated in three of the four themes in Figure 5.



Overall, local authorities have coped very well with delivering the first year of SR10.

- 86% of authorities were rated green for **key indicators of financial performance** for 2010–11, and this has increased to 96% for 2011–12. For each category in this thematic area the

trend has been an increasing level of green ratings and reducing levels of amber ratings, with liquidity receiving the lowest overall rating (87%). While for many authorities their Treasury Management Strategy is leading to a planned reduction in liquidity, and borrowing headroom provides a degree of confidence for the medium-term, authorities will need to ensure that their liquidity is carefully monitored, for example in the collection of council taxes and business rates during challenging economic times. The overall position indicates that local authorities are both treating the financial challenges being faced seriously, and delivering against their financial plans.

- Local authorities demonstrated good **financial governance** during our 2010–11 reviews, with 86% receiving green ratings. This has increased to 92% for 2011–12. Local authorities will need to continue to ensure financial governance arrangements remain robust. Given the generationally significant financial challenges facing authorities, it will be particularly important that the chief financial officer is a key member of the authority’s leadership team. This theme has the first sub category to receive a red rating (Adequacy of Reporting) and it will be critical that financial information is reported accurately, at the right frequency, and in a format that ensures effective monitoring and decision making. This includes where services are not delivered in-house, which will be an increasing trend for the sector.
- Our 2010–11 reviews indicated that the weakest thematic area was **financial controls**, with 71% of authorities receiving a green rating. Our 2011–12 reviews indicate an improvement, with 83% of our sample receiving a green rating. However, this is the joint lowest overall rating, along with strategic financial planning. A key risk to be managed in this area continues to be embedding the changes resulting from reductions in finance staff and the associated increase in financial responsibilities of service managers and budget holders. Local authorities also need to improve the management information relating to the reporting of savings programmes, in particular with the inclusion of greater detail on the use of countervailing savings, so that key stakeholders can better understand the impact on service delivery and policy decisions, where such alternative savings are being applied to pre-agreed targets.

- Local authorities demonstrated strong **strategic financial planning**, during our 2010–11 review, with 93% in our sample receiving a green rating. This declined to 83% for 2011–12, the only thematic area that saw a fall in the overall green rating. While this remains at a high level overall, the reduction highlights the increasing difficulty local authorities face in planning for the medium-term in what remains a greatly challenging and uncertain period. It remains critical that authorities improve their scenario planning and the use of sensitivity analysis on key assumptions in their financial models. As we noted in our 2011 report, we believe authorities can learn directly from the financial modelling analysis required by Foundation Trust applicants in the NHS.

## **Comparison to the health sector**

We undertook similar reviews of a sample of NHS trusts and primary care trusts (PCTs) for both 2010–11 and 2011–12.

Our 2011 report observed that, despite NHS funding levels being maintained by the Government, health bodies received lower ratings than local authorities for 2010–11, with significantly lower levels of green ratings across themes, and with no green ratings for key indicators of financial performance. There has been some improvement for 2011–12. For example, and unlike local authorities, strategic financial planning for health bodies has improved. Health bodies have also seen an improvement for KPIs and the overall position for financial governance has stabilised. However, the overall ratings remain significantly lower than the overall local authority ratings. As we noted in our 2011 report, the underlying causes of these findings predate SR10, and relate to long-term structural issues, particularly within the acute sector. Like local government, performance is varied, but the higher performing trusts are often very good at scenario planning and sensitivity analysis as a response to volatile demand-led costs and income, although the sector as a whole has difficulty in delivering to these budgets.