

Consultation

# local authority financial resilience index

# foreword

Local government has faced unprecedented financial challenges in recent years that are likely to remain well into the next decade. On a positive note, local authorities operate within a strong framework of accountability which ensures effective management of resources. English local government, for example, spends 25% less in real terms than eight years ago, having lost half of the grants received from central government, and yet continues to deliver core services. Councils have a historic track record of managing their balance sheets more actively than other parts of the public sector through, for example, creating pension funds to manage superannuation liabilities and operating under a prudential framework for strategic investment.

However, the recent National Audit Office report on financial sustainability in local authorities, published following the crisis at Northamptonshire County Council, indicates that there is a heightened risk of more councils over the next four years falling into special financial measures as a result of the unrelenting pressure on budgets. There are a number of tools already available to assist councils in recognising and dealing with an approaching serious financial situation including the S114 statement and CIPFA believes that timely use of these statements will be more effective in stabilising councils before they go over the cliff edge. Such use would hopefully avoid the type of failure we have seen in Northamptonshire County Council, where it is clear from the independent inspector's report that too little action was taken too late.

In response to the challenges outlined above, CIPFA is strengthening its range of guidance, tools and services to promote better financial management and provide an early warning system to senior officers and members. Through the development of a new Financial Management Code, we aim to support good practice in the planning of sustainable finances.

We are reviewing the continuing professional development requirements of chief financial officers at this time of heightened risk, and will also provide a new range of accredited learning packages for managers, elected members and leadership teams to embed the new Financial Management Code.

Another part of this overall package is a resilience index, which CIPFA will now produce as an open access free resource annually or when significant new data is available. The resilience index is not a performance table of service outcomes or quality, and is not a comment on the quality of leadership in councils. It aims, however, to be an authoritative measure of councils' financial resilience, drawing on publicly available information, intended to provide an early warning system where it is needed so that action can be taken at a local level in a timely manner. CIPFA believes that good governance best occurs when it is supported by well-founded evidence which is discussed objectively and we believe it is in all councils' and taxpayers' interests that a comparative resilience index is produced from which local government and its external auditors can draw.

## **Rob Whiteman**

Chief Executive

CIPFA, Chartered Institute of Public Finance and Accountancy

# 1. introduction: an index of financial resilience for English councils

- 1.1 CIPFA is consulting on its proposed publication of an index of resilience of English councils. This paper sets out the objectives of the index, describes our proposed methodology, illustrates how the response will be displayed and explains how to respond to this consultation.
- 1.2 The decision to develop an index is driven by CIPFA's desire to support the local government sector as it faces a continued financial challenge. The index, based on publically available information, will provide an assessment of the relative financial health of each English council. As with all of CIPFA's analytical products, the index will not be a predictive model but a diagnostic tool – designed to identify those councils displaying consistent and comparable features that will highlight good practice, but crucially, also point to areas which are associated with financial failure. The information for each council will show their relative position to other councils of the same type. Use of the index will support councils in identifying areas of weakness and enable them to take action to reduce the risk of financial failure. The index will also provide a transparent and independent analysis based on a sound evidence base which should be more useful than unattributed speculation informed by little more than anecdote.
- 1.3 We propose to develop and publish the index for every county, district, metropolitan borough, unitary authority and London borough in England although there will be a slightly different and simplified methodology for those councils that do not have a social care responsibility. CIPFA will consider extending the geographical coverage of the index to Scotland, Wales and Northern Ireland over time.

## 2. methodology

2.1 Our proposed approach draws on CIPFA's evidence of the factors associated with financial stress. These include<sup>1</sup>:

- running down reserves
- failure to plan and deliver savings in service provision
- shortening medium-term financial planning horizons.
- gaps in saving plans
- departments having unplanned overspends and/or undelivered savings.

2.2 Additionally, we have held discussions with senior practitioners and sector experts. These conversations have elicited a number of additional potential factors. These include:

- the dependency on external central financing
- the proportion of non-discretionary spending – eg social care and capital financing - as a proportion of total expenditure
- an adverse (inadequate) judgement by Ofsted on Children's services
- changes in accounting policies (including a change by the council of their minimum revenue provision)
- poor returns on investments
- low level of confidence in financial management.

2.3 Not all of these factors can easily be measured, and certainly not in an objective way. To develop the index we have established a set of principles:

- measurements need to be consistent across all councils within a tier
- measures should be objective
- the methodology must be transparent
- we should use the latest available reliable measures.

The broad approach is to calculate a council's score on a range of indicators. The table below shows the proposed indicators for the first publication of the index – together with an explanation of its inclusion. The majority of the data will be drawn from the General Fund Revenue Outturn (RO) form. Other data sources are shown in the table.

<sup>1</sup> Building financial resilience: managing financial stress in local authorities, CIPFA 2017

**Table 1: Indicators and sources**

	Indicator	Where will the data be sourced	Why is this indicator included	Comments
1	The level of total reserves excluding schools and public health as a proportion of net revenue expenditure.	Data will be drawn from the RO returns. For councils with a social care responsibility, we will include data for the latest year drawn from unaudited statements of accounts.	A low level means that there is little scope to draw on reserves should the budget not be met.	
2	The percentage change in reserves, excluding schools and public health, over the past three years.	Data will be drawn from the RO returns. For councils with a social care responsibility, we will include data for the latest year drawn from unaudited statements of accounts.	If a council is reducing its reserves it may not be achieving necessary savings to balance its budget.	
3	The ratio of government grants to net revenue expenditure.	RO returns.	If a council has a higher dependency on central government financing, it may face greater financial pressures than those with more local resources.	We propose to show also the ratios of retained business rates and council tax but they will not be used in the index calculation.
4	Proportion of net revenue expenditure accounted for by children’s social care, adult social care and debt interest payments.	RO returns.	A high proportion suggests that a council has little headroom to make cuts in expenditure on more discretionary expenditure.	This measure is not relevant for councils without a social care responsibility.  The three elements will be also be shown separately but only the total will be included in the composite index.
5	Ofsted overall rating for children’s social care.	Ofsted management information.	Councils with an “Inadequate” rating are likely to be under considerable pressure to increase spending in this area.	This measure is not relevant for councils without a social care responsibility.
6	Auditor’s VFM judgement.	Public Sector Audit Appointment’s summary of the results of audit.	An adverse or “except for” judgement may be indicative of poor financial management within a council.	

# 3. scoring the index

3.1 These six indicators are a mix of continuous and categorical variables. To produce a council’s score on each continuous measure, we propose to adopt the following approach.

Step 1: Identify the highest and lowest values within the comparator group.

Step 2: Assign a score of 0 to the lowest performing council and 1 to the highest performer.

Step 3: For the each council, the indicator score is calculated as:

$$\frac{\text{council value} - \text{minimum value}}{\text{maximum value} - \text{minimum value}}$$

3.2 For the categorical variables, the categories are given a numerical value and the same calculation made.

The result of these calculations is a relative score on each measure for each council which, for ease of interpretation, will be rescaled so the median score is 100.

# 4. combining the scores

4.1 To produce the overall index score, the individual measure scores are combined together as a weighted average. The proposed initial set of weights for councils with a social care responsibility are shown in the following table and reflect our view on the relative importance of each indicator in assessing financial health.

4.2 For councils without a social care responsibility, the weights for social care will be set to 0 and the other weights will be increased so that the weights sum to 1.

4.3 The outcome is a single score where the lower the score the more factors associated with financial failure are present. Again the overall score will be rescaled so the median is equal to 100.

**Table 2:**

Indicator	Weight
Level of reserves	0.25
Change in reserves	0.25
Grants to expenditure ratio	0.10
Social care and debt financing ratio	0.15
Ofsted inspection score	0.15
Auditor’s VFM judgement	0.10

# 5. presentation

- 5.1 The data will be presented in two ways. CIPFA will generate a table showing, for each council, its overall score and the scores of the individual indicators that make up this score. To aid interpretation we will colour code the results to indicate the different levels of risk for each councils.
- 5.2 In addition, we will produce an interactive Excel tool to enable councils and others to explore the data. This will generate a dashboard showing a council's relative

score on each measure – including the components which are not part of the composite indicator. The tool will also allow users to display a council's ranking in the indicators as well as its raw score. An illustrative example of the dashboard is shown on the next page. The tool will be freely available on the CIPFA website allowing anyone to access the results of this analysis. We will also provide a summary analysis of tiers and geographies – but this tool will allow for users to make their own comparisons.

# 6. consultation questions

- 6.1 CIPFA welcomes views on the development of this index. Specifically, we would like respondents to address the following questions
  - a. Are the proposed indicators the right ones – are there other measures that should be included or ones omitted?
  - b. Is the method for combining the indicators to produce a composite indicator appropriate? Are the weights, particularly the greater weighting on reserves reasonable?
  - c. Is the proposed presentation, including both the summary and the individual council dashboard, the right way to present the data?
  - d. Do you have any comments on CIPFA's view that to aid transparency the full analysis should be freely available on CIPFA's website?
  - e. Available data tends by its nature to be retrospective, what forward looking indicators would you also see as useful to include to support the index?

# 7. responding to the consultation

You can submit your response to the consultation by visiting the CIPFA website at [www.cipfa.org/resilienceindexconsultation](http://www.cipfa.org/resilienceindexconsultation) or writing to us at [resilienceindex@cipfa.org](mailto:resilienceindex@cipfa.org)

Resilience Index Consultation  
Research and Analytics  
CIPFA  
77 Mansell St  
London  
E1 8AN

CLOSING DATE FOR RESPONSES  
24 AUGUST 2018

# financial resilience index analysis

Authority: Barchester  
Year: 2016-17

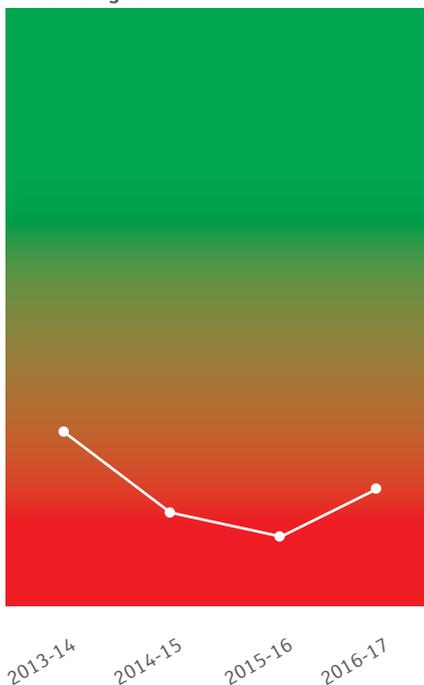
Comparator Group: London Boroughs  
Distribution: Raw

	Worst performing	Best performing	Max	Min	Authority
Total - schools - PH reserves /net exp			£1,817	£124	£463
Earmarked Reserves (line 915) /net exp			£1,532	£89	£291
Unallocated Reserves (line 916) /net exp			£558	£35	£172
School Reserves Variation (line 811) %			124.4%	-94.3%	-24.7%
Public Health Reserves Variation (line 814) %			274.8%	-100.0%	-79.5%
Earmarked Reserves Variation (line 815) %			95.2%	-62.7%	-4.3%
Unallocated Reserves Variation (line 816) %			109.8%	-71.3%	-28.8%
Total - schools - PH reserves variation /net exp £k			35885.3%	-15107.9%	-15107.9%
Revenue Support Grant (line 851) /net exp			£165	£761	£412
Council Tax Requirement (line 890) /net exp			£699	£52	£272
Council Tax Requirement/RSG			£306	£4,234	£661
Retained Income from Rate Retention (line 870) / net exp £k			£0	£0	£0
Other items (line 880) £			£1,718	£7,274	£1,067
Children Social Care Service Expenditure (line 330) /net exp			£355	£19	£355
Adult Social Care Service Expenditure (line 360) /net exp			£545	£59	£279
Total Social Care Expenditure + Interest Payments /net exp			£861	£77	£633

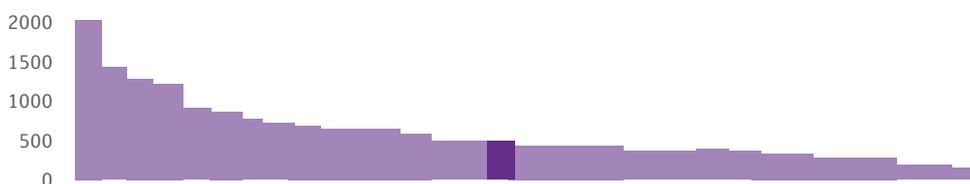
Auditors VFM Judgement
Unqualified

Social Care Ratings	
Help and protection	
Requires Improvement	
Children looked after and achieving permanence	
Requires Improvement	
CLA sub: adoption performance	
Requires Improvement	
CLA sub: experiences and progress of care leavers	
Requires Improvement	
Leadership, management and governance	
Requires Improvement	
LSCB overall effectiveness	
Requires Improvement	

Trend Analysis



Group Overall Performance	
Comparator 1	160.7
Comparator 2	128.0
Comparator 3	127.4
Comparator 4	120.2
Comparator 5	118.7
Comparator 6	116.2
Comparator 7	115.5
Comparator 11	108.0
Comparator 12	107.7
Comparator 13	107.4
Comparator 15	103.3
Comparator 16	102.2
Comparator 17	99.5
Comparator 18	99.4
Comparator 19	99.3
Comparator 20	96.8
Comparator 21	93.6
Comparator 22	93.4
Comparator 23	92.4
Comparator 24	90.4
Barchester	84.0
Comparator 26	83.4
Comparator 27	78.4
Comparator 28	77.9
Comparator 29	75.8
Comparator 30	75.5
Comparator 31	71.0
Comparator 32	66.5
Comparator 33	61.2





Registered office:

77 Mansell Street, London E1 8AN

T: 020 7543 5600 F: 020 7543 5700

[www.cipfa.org](http://www.cipfa.org)

The Chartered Institute of Public Finance and Accountancy.  
Registered with the Charity Commissioners of England and Wales No 231060  
Registered with the Office of the Scottish Charity Regulator No SC037963