CIPFA The Chartered Institute of Public Finance & Accountancy

An introductory guide to

local government finance

2017 edition

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Preface

The continuing political uncertainty since the referendum vote to leave the EU has had important implications for local government. The future trajectory of government policy, notably for business rate reform, remains unclear. As a consequence, the challenge of rendering local government services financially sustainable remains to be addressed. This challenge is becoming more difficult with the increasing pressures of health and social care and the lack of political consensus on a way forward. An understanding of local government finance remains essential to understand these important policy debates. This understanding will be supplied by reading this publication.

Contents

CHAPTER ONE

A brief introduction to local government

Local government in England is a patchwork of different types of council. There is a mixture of single-tier councils, in which one council provides all the services for an area, and two-tier councils, in which these services are shared between two councils, known as an upper-tier council and a lower-tier council. In addition, police and fire services also come within the local government sector.

Greater devolution in England has seen an increase in the number of combined authorities. The Greater Manchester Combined Authority was at the forefront of this change but further devolution has followed, including for London in the spring 2017 Budget.

In Wales, there is only a single tier of local government, plus police and fire services.

As well as the principal local authorities, in many areas of England and Wales there are also local councils. These may be parish, town or community councils, which provide a much smaller number of services within a small local area.

The following table illustrates the local government structure for single- and two-tier areas in England and Wales.

England outside London		London	Wales
County councils	Metropolitan councils and unitary councils	Greater London Authority	Unitary councils
District and borough councils		London borough councils	
Police and fire authorities*			

** Police services are provided by the Greater London Authority (GLA) in London and fire services are still the responsibility of some upper-tier authorities.*

Councils provide a whole range of services, with responsibility split between upper- and lower-tier councils in two-tier areas. The following table shows some of the services provided by local government and highlights which tier has responsibility for them in two-tier areas. Councils do, however, work increasingly in partnership with each other and while an individual council will retain responsibility for provision of services, other councils or organisations may provide these on its behalf. Combined authorities are an example of how this can be done. The drivers behind this are better use of resources and improved provision for the customer.

Upper tier		Lower tier	
Education	Social care	Housing	Planning
Highways*	Libraries	Waste collection	Street cleaning
Country parks and footpaths	Trading standards	Environmental health	Museums and leisure centres
Economic regeneration*	Waste disposal	Parks	Economic regeneration
Concessionary fares and public transport*	Planning strategy*	Markets and town centres	Parking
	Registrars		
	Public health		

** Provided by the GLA in London, which also has responsibility for police and fire services.*

Councils currently receive funding for the services they provide from local residents and businesses through council tax and business rates and from central government through grants for specific purposes and Revenue Support Grant for general purposes. Central government issues regulations on how councils raise and spend money to provide services. These are described in more detail in the following chapters.

The devolution agenda has seen a rise in the debate around tax-raising powers with many councils wanting fiscal control to move away from Whitehall. Although in England there has been some devolution of business rate income the current system is still highly centralised. The political uncertainty following the 2017 election has for the moment halted moves towards a further decentralisation of local government finance.

Finally it should be noted that the financial year for all councils is 1 April to 31 March.

CHAPTER TWO

The revenue budget and resources

THE REVENUE BUDGET

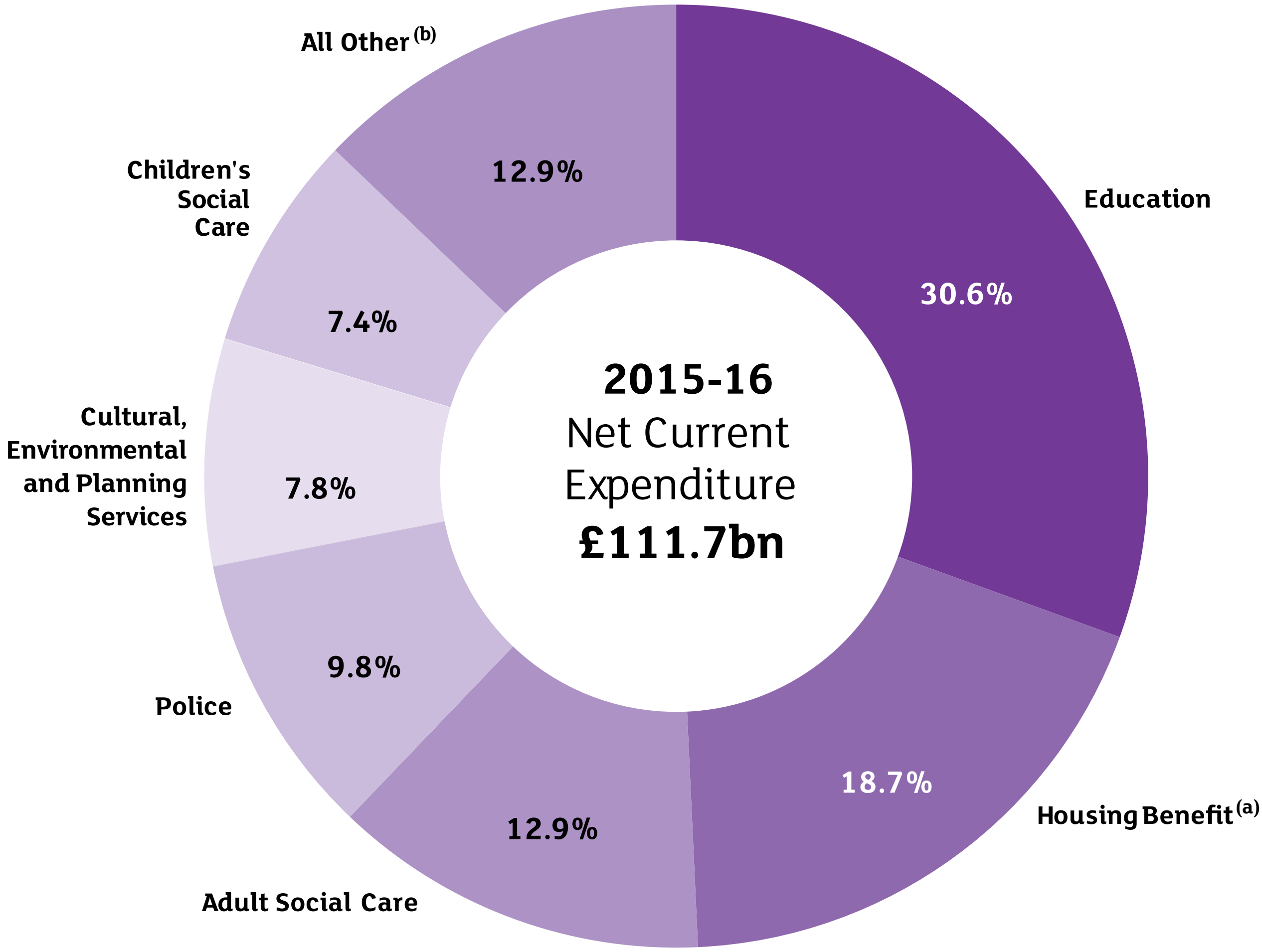
The revenue budget is the term used to describe the amount that a council spends on its day-to-day running of services. This includes wages and salaries, property and transport running costs and payments to suppliers.

In addition to the running costs of services, councils have to fund the costs of borrowing money to pay for their capital assets. Councils also need to meet the costs of certain other local service providers, such as the Environment Agency for flood prevention work, through what are known as levies. Once all these things are taken into account, along with specific grants, a figure known as 'net revenue expenditure' is reached.

The money a council spends on investing in new buildings, infrastructure and equipment is known as the capital budget and is covered later in this guide.

Information released in November 2016, Local Authority Revenue Expenditure and Financing England: 2015 to 2016 Final Outturn, shows how this expenditure is allocated across local government services.

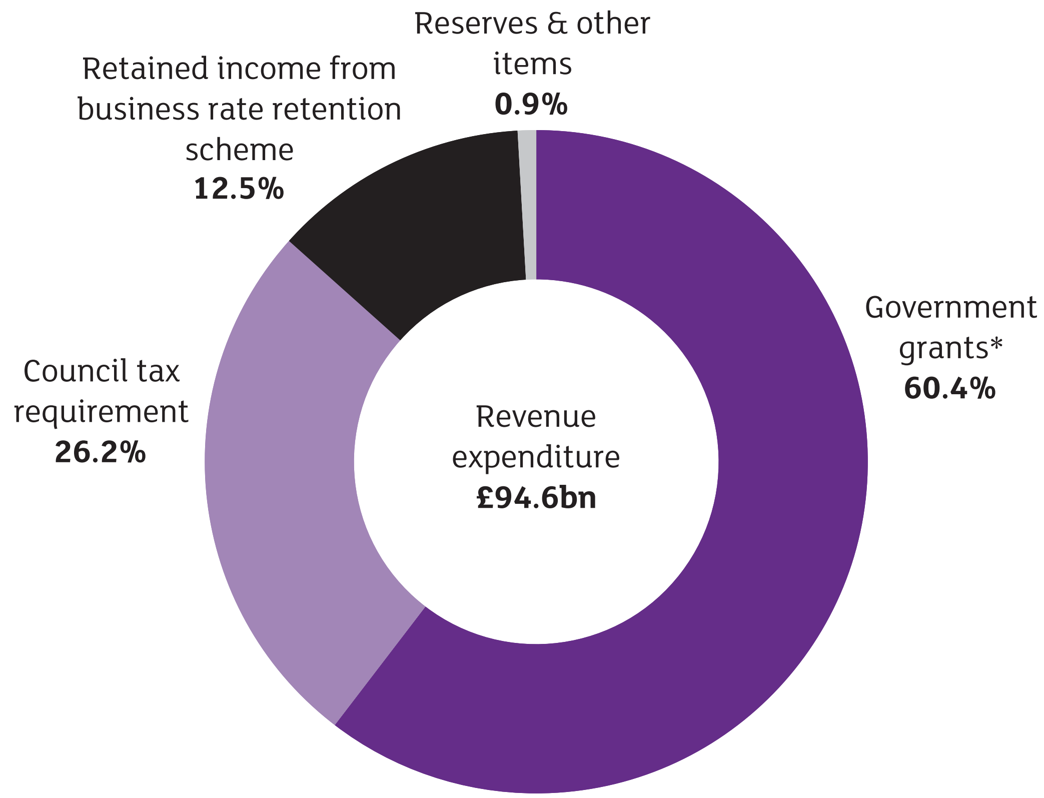
Proportion of total net expenditure by service, England, 2015/16



(a) *Housing benefit includes mandatory rent allowances and rent rebates and non-mandatory housing benefit payments.*

(b) *'Other' includes 'highways and transport', 'public health', 'fire and rescue', 'central services', 'other services' and 'precepts, levies, trading accounts and adjustments' excluding housing benefit.*

Financing of revenue expenditure, England, 2015/16



** 'Government grants' includes 'Local Services Support Grant (LSSG)', 'Specific grants inside Aggregate External Finance (AEF)', 'Revenue Support Grant' and 'Police Grant'. Since 2013/14 these specific grants inside AEF have included Public Health Grant, Local Council Tax Support Grant and the central share of non-domestic rates.*

SPECIFIC GRANTS

Councils receive a number of specific grants from central government to support government priorities. The table below sets out income from the five largest specific grants in England. The trend is to move away from specific grants and include funding in the main settlement which can be spent according to local priorities.

Main specific grants – England, 2015/16

Grants inside aggregate external finance	£m
Dedicated Schools Grant (DSG)	28,065
Public Health Grant	3,032
Pupil Premium Grant	1,655
New Homes Bonus	1,108

Source: Local Authority Revenue Expenditure and Financing: 2015-16 Final Outturn, England

COUNCIL TAX REQUIREMENT

From the net revenue expenditure figure any use of council reserves (a topic covered later) is subtracted to get to a budget requirement figure that is then funded from general government grant, non-domestic rates and council tax.

COUNCIL TAX

Council tax is collected from residents within a council's area based on the value of the property they live in. Council tax was introduced in 1993 to replace the community charge (or poll tax). For the purpose of council tax each property is assigned to one of eight bands, A to H, based on their value in 1991. The value of each property is assessed by the Valuation Office Agency, an agency of central government. For properties built after 1991, value is assessed as if the property had existed in 1991. Residents who do not agree with the council tax band their property has been placed in have a right of appeal.

In Wales, the property values relating to each band were reassessed and updated in 2005 based upon 2003 property values. This process is known as council tax revaluation. There has been no revaluation in England.

The band a property is placed in determines how much council tax will be paid relative to other properties in the same council area. For example, a Band A property will pay two thirds of the amount of council tax paid by a property in Band D, while a property in Band H will pay double. The following table sets out the property values that relate to each of the council tax bands and the relative amounts of council tax that will be paid.

Band	English values	Welsh values before 2005	Welsh values from 2005	Relative council tax
A	Less than £40,000	Less than £30,000	Less than £44,000	$^{2}/_{3}$
B	£40,001 to £52,000	£30,001 to £39,000	£44,001 to £65,000	$^{7}/_{9}$
C	£52,001 to £68,000	£39,001 to £51,000	£65,001 to £91,000	$^{8}/_{9}$
D	£68,001 to £88,000	£51,001 to £66,000	£91,001 to £123,000	1
E	£88,001 to £120,000	£66,001 to £90,000	£123,001 to £162,000	$^{11}/_{9}$
F	£120,001 to £160,000	£90,001 to £120,000	£162,001 to £223,000	$^{13}/_{9}$
G	£160,001 to £320,000	£120,001 to £240,000	£223,001 to £324,000	$^{5}/_{3}$
H	Over £320,000	Over £240,000	Over £324,000	2

The level of council tax can be reduced in certain circumstances, including:

- a discount of 25% when fewer than two people occupy a property. It should be noted that certain people are excluded when calculating the number of people in a property, including under 18s and students
- a reduction of one council tax band for people living in houses that have had disabled adaptations made to them
- discounts for those on low incomes and pensioners. Each council now has its own local scheme to determine who can apply for a discount based on income. Pensioners are protected under the national scheme.

The requirement for councils to have discount schemes for those on low income was introduced in 2013/14. Previously there was a national scheme for council tax benefit that was part of the benefits system. Since 2013/14 each billing authority has been required to deliver its own local scheme with some freedom to decide on the criteria against which people will be assessed. Because the council tax discount is converted to a percentage reduction in the council tax base (see below), it automatically makes a proportionate impact on the major and local precepts.

Council tax is collected by local billing authorities; these are unitary authorities, district councils, metropolitan councils and London boroughs. Other local authorities, including county councils, police and fire authorities and the GLA, raise money from the council tax by setting a precept which is collected on their behalf by the billing authority. The precept is the formal term given to the total amount an authority other than a billing authority wishes to raise from the council tax. This amount is converted to an amount of council tax and shown separately on bills.

Calculating the Council Tax

The council tax is calculated by subtracting the amount of business rates and Revenue Support Grant that a council expects to receive from its budget requirement. The balance is left to be funded by the council tax and the actual council tax is calculated by dividing this amount by the council tax base.

The council tax base is calculated by converting the number of dwellings in each band to Band D equivalents, for example each house in Band H is equivalent to two Band D houses and each Band A house is equivalent to two thirds of a Band D house. From this amount the value of any discounts is subtracted; for example, if a single person’s tax discount (equivalent to 25%) is awarded to four houses in the same band, this would reduce the tax base for that band by one. The following example shows a very simplified version of how this works.

Band	Number of properties	Reduction due to discounts	Adjusted number of properties	Ratio	Band D equivalent
A	3,000	1,200	1,800	$^{2}/_{3}$	1,200
B	4,000	1,300	2,700	$^{7}/_{9}$	2,100
C	6,000	1,500	4,500	$^{8}/_{9}$	4,000
D	4,500	1,000	3,500	1	3,500
E	3,200	500	2,700	$^{11}/_{9}$	3,300
F	1,950	150	1,800	$^{13}/_{9}$	2,600
G	1,850	50	1,800	$^{5}/_{3}$	3,000
H	920	20	900	2	1,800
Total					**21,500**

In this example the tax base for the area is 21,500 Band D equivalents. The Band D council tax is calculated by dividing the amount to be raised from council tax by the council tax base. The council tax for other bands is then calculated by multiplying the Band D council tax by the relative ratio for each band; for example, if the Band D council tax is £900, the Band A council tax will be two thirds of this amount or £600.

This calculation will be carried out by the billing authority, major preceptors and local billing authorities to come to a final council tax figure that citizens will pay. The example below shows the calculation for an area with a police and crime commissioner, a county council, a district council and a parish council. The council tax base is higher for the police and crime commissioner and the county council as these cover several district council areas and lower for the parish council as there will be several within the district council area.

Council	Precept/ amount to be collected from council tax	Tax base	Band D council tax
	£		£
County council	225,000,000	250,000	900
Police and crime commissioner	30,000,000	250,000	120
District council	4,300,000	21,500	200
Parish council	75,000	1,500	50
Total to be paid by council tax payers			**1,270**

Council tax can be paid either in a lump sum or in instalments, usually by direct debit. Government regulations make payment by ten instalments the default option for payment.

Billing authorities are responsible for collecting council tax and paying over the major and local preceptors’ shares. They are also responsible for dealing with any arrears and taking action against non-payers, which includes the ability to make discretionary hardship payments to those genuinely struggling to meet their bills.

Council Tax Increases

Consecutive governments have been concerned about the level of increases in council tax and have sought to limit the amount by which council tax is allowed to increase. Initially this was done through capping under which councils were given specific limits to the amount by which their budgets could increase. This system of crude and universal capping was abolished in 1999 but the secretary of state retained reserve powers.

For England, since 2012/13, council tax referendum rules have been in place. Under these rules, if a council increases its council tax above a pre-announced percentage, that council will have to organise a referendum of council tax payers to approve the increase. The referendum limit for 2015/16 was 2%. Councils are unlikely to risk going to a referendum because this would take place after the budget setting and council tax billing processes have finished and councils would risk having to meet the cost of re-billing if tax payers vote no. However in 2015 Bedfordshire Police asked for additional funds equivalent to 48p per week on a Band D property; this was above the referendum limit and a vote was held. The public chose to reject the tax rise.

As well as using referendums to limit council tax increases, the government has also made a grant available to those councils that implemented a council tax freeze, with eligible councils receiving grant equivalent to the income that would have been raised by a small increase in council tax. 2015/16 was the final year for the allocation of the council tax freeze grant.

In the 2015 Autumn Statement councils were given the flexibility to include a 2% increase for adult social care. In its annual Council Tax Survey, CIPFA found that council tax in England (excluding London) rose by an average of 3.6%, adding £54 to the average Band D bill. However, Greater London council tax payers saw an average increase of just 0.6% or £8.04.

THE COLLECTION FUND

Because a billing authority collects council tax on behalf of all the councils in its area, there is a need to avoid mixing up the true income due to the billing authority with income that is merely passed straight on to its preceptors. The collection fund is the way this is done. All council tax income is paid into the collection fund and the payments are made from the collection fund into the billing authorities' individual accounts and to the major preceptors. The government does not want the income councils receive during the year to vary too significantly as this may cause problems for budgeting purposes, and so has made regulations to achieve this through the collection fund.

The amount that individual councils receive from the collection fund is fixed at the level of the precept or the amount that is projected when the council tax is set. This amount is paid out of the collection fund regardless of how much council tax is collected during the year. If more council tax is collected than expected, this creates a surplus on the collection fund; if less is collected, this creates a deficit on the collection fund. The surplus/deficit on the collection fund is shared out to the individual councils in the following years and taken into account in those budget calculations.

The collection fund is also used to collect and pay out amounts related to business rates.

BUSINESS RATES

Business rates are payable by businesses based on the rateable value of the premises they occupy. Valuations are carried out by the Valuation Office Agency on a five-year cycle. The last valuation list came into existence in 2010 and listed the rateable value of all business properties. The rateable value broadly represents the annual rent the property could have been let for on the open market on a particular date, on full repairing and insuring terms. For the current rating lists, this date was set as 1 April 2008.

Councils are responsible for calculating actual rates bills and for collecting rates and will use the rateable value in working out how much businesses have to pay. The actual rate bill is calculated by applying the rate multiplier (a rate in the pound) to the rateable value and then deducting any reliefs that are applicable. The multiplier is set by the DCLG in England and by the Welsh Government in Wales.

The business multiplier for 2017/18 is:

- England = 47.9p in the pound
- small businesses in England = 46.6p in the pound
- all businesses in Wales = 49.9p in the pound.

For England, a small business is one where the total rateable value is under £18,000 (or under £25,500 in London). For example, a property with a rateable value of £12,000 in England would have an annual rates bill of **£12,000 x 0.499 = £5,988**.

In the 2016 Budget, it was announced that firms occupying property with a rateable value of £12,000 or less would pay no business rates from 2017.

Some businesses may be eligible for small business relief or charitable discounts, which can affect the amount of rates they pay. In addition, billing authorities are able to grant discretionary relief to individual businesses, for example to promote town centre regeneration.

Until 2013/14, councils merely collected business rates for redistribution by central government. All the business rates (or non-domestic rates as they were then called) collected nationally were passed back to councils as part of their overall funding allocation from central government. As this funding allocation is determined by a funding formula, some individual councils receive back less in funding than they had collected in business rates. In an important change, from 2013/14 councils in England, other than police and crime commissioners, are able to keep a portion of the business rates raised in their areas. The system remains unchanged in Wales.

Business Rate 100% Retention

Prior to the 2017 election, the government was committed to allow local authorities to retain 100% of business rate income from 2019/20. Following the election, development of the details of the scheme has stopped until the future of the policy is made clear.

Business Rate 50% Retention – England Only

Since April 2013, councils have been allowed to keep a proportion of the business rates they collect from businesses in their area. The proportion a council is allowed to keep depends upon the type of local authority. In all areas, half of business rates have to be paid over to central government. Billing authorities continue to collect all of the business rates in their area on behalf of central government and the major precepting authorities, which, with the exception of police and crime commissioners, are the same as for council tax.

The shares of total business rates each type of local authority is allowed to keep are set out in the following table.

District councils	40%
County councils (with responsibility for fire)	10%
County councils (where there is a separate combined fire authority)	9%
Unitary and metropolitan councils (with responsibility for fire)	50%
Unitary and metropolitan councils (where there is a separate combined fire authority)	49%
Combined fire authorities	1%
London boroughs	30%
Greater London Authority	20%

Because the amount of business rates an individual council is able to collect will vary enormously depending upon location and the characteristics of the council, the government introduced a system of top-ups and tariffs to redistribute business rates. Councils with a relatively high level of business rates pay a tariff into a national pot which is used to pay top-ups to those councils with relatively low levels of business rates. The level of these top-ups and tariffs was set by the 2013/14 local government finance settlement, and is set for a period of at least seven years, although both top-ups and tariffs will increase by inflation over that time.

In order to prevent councils having to drastically cut services as a result of a significant fall in business rate income and to provide some protection against major economic shocks, the government introduced a safety net mechanism to ensure that no council will experience a fall in business rate income of more than 7.5% in any one year. This safety net is paid for by a levy on what the government deems to be 'excessive growth'. Councils whose business rates increase by more than inflation have to pay over a greater proportion of business rates to government.

The levy rate for each council is set as part of the local government finance settlement. To ensure that an incentive for growth is retained, the levy rate is capped at 0.5, ie all councils are able to keep at least half of the growth in their local share of business rate income.

The amount of business rates a local council will take into account when setting its budget each year is set when the billing authority completes its estimate of business rate income for the following year in January and completes a return to government (called the NNDR1 form) setting out this amount. This also fixes the amount that the council will pay over to government.

Business rate income is paid into the collection fund, administered by the billing authority, as it is collected from businesses. The collection fund then makes payments out to the billing authority general fund, the major preceptors and government, based on the NNDR1 estimate. If more income is received than estimated, this creates a surplus on the collection fund, or if less is collected, a deficit, and this is paid over to the individual councils and government the following year.

Where a council's estimate is so low that the safety net becomes payable, payments are made on account by government during the year. Any levy payments and the difference between estimated and actual safety net payments become payable at the end of the financial year, although the actual cash is paid over in the following financial year.

REVENUE SUPPORT GRANT

Revenue Support Grant is a grant paid by government to support councils' general expenditure. There are no restrictions on how it is to be used (within a council's legal powers) and the amount each council will receive is set out in the local government finance settlement. While 100% business rate retention remained government policy the intention had been to phase out Revenue Support Grant by 2019/20 by replacing it with the retained rates. Following the 2017 election the future direction of this policy is unclear.

CHAPTER THREE

Capital budgets and resources

CAPITAL BUDGETS

A council's capital budget covers the money it spends on investing in buildings, infrastructure and expensive pieces of equipment. Capital spending by councils is mainly for buying, constructing or improving physical assets such as:

- **buildings** – schools, houses, libraries, museums, police and fire stations, etc
- **land** – for development, roads, playing fields, etc
- **vehicles, plant and machinery** – refuse collection vehicles, fire engines, police cars, etc.

It also includes grants and advances made to the private sector or the rest of the public sector for capital purposes, such as advances to housing associations. In order to count as capital expenditure, new assets or additions to assets must have a life of more than one year.

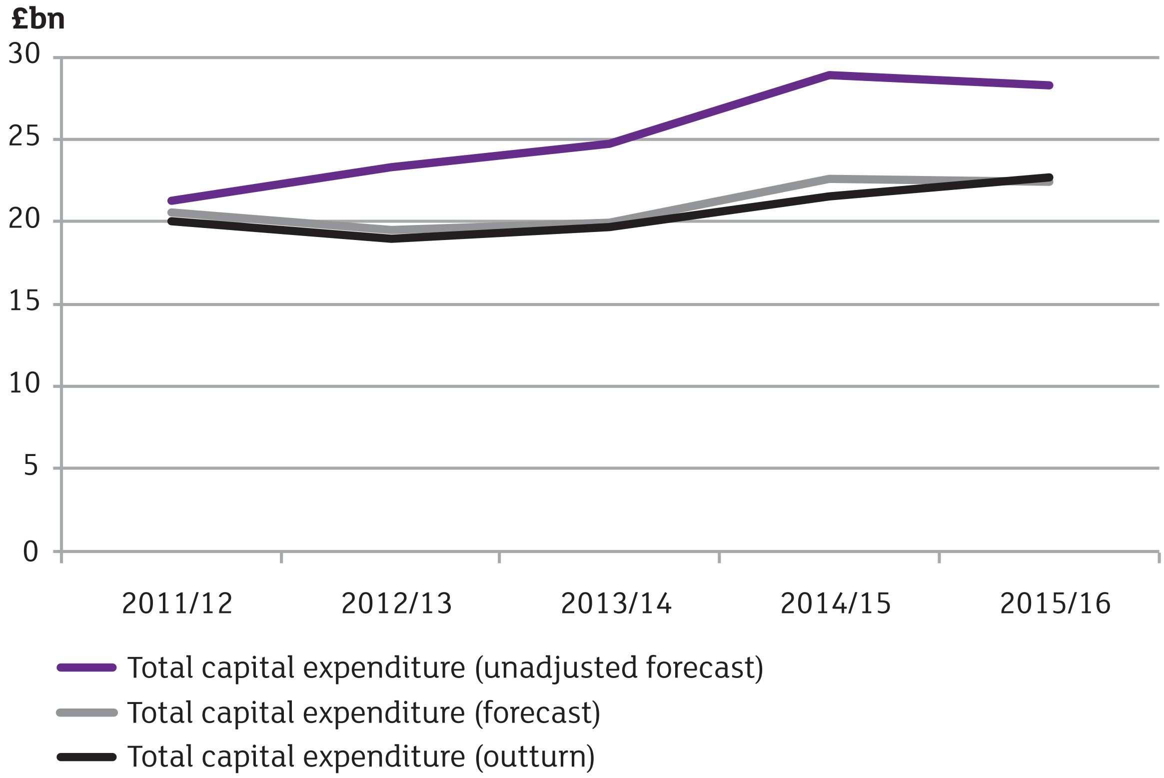
At the discretion of the secretary of state, certain revenue costs can be treated as if they are capital costs. This process, known as a capitalisation direction, is subject to an annual application process and is typically used for one-off items such as redundancy costs and meeting the costs of equal pay claims. The secretary of state can also extend the definition of capital expenditure using regulations.

Councils in England spent £22.6bn on new assets and additions to existing assets in 2015/16, an increase of 5.2% on the £21.5bn spent in 2014/15. In Wales, councils spent £2.0bn in 2015/16, an increase of £1bn or 98% over the previous year mainly due to the one-off housing revenue account subsidy buyout of exceptional size.

Capital receipts are received when a council sells capital assets. In 2015/16 councils in England received capital receipts of £3.6bn, an increase of 19.4% from the £3.0bn in 2014/15. In 2015/16 councils in Wales received capital receipts of £67.9m, a decrease of 17.5% from the £82.3bn in 2014/15.

The chart below shows capital expenditure and capital receipts for the period 2011/12 to 2015/16.

Capital expenditure and receipts – England and Wales 2011/12 to 2015/16



Source: National Statistics, Local Authority Capital Expenditure and Receipts: England 2015/16 Final Outturn, September 2016 and Welsh Government Statistical Release, Local Authority Revenue and Capital Outturn Expenditure: 2015/16, October 2016

The chart also shows the expenditure excluding the GLA as the GLA tends to distort the total council capital spending figures as it includes expenditure on large infrastructure projects by Transport for London.

FINANCING OF CAPITAL EXPENDITURE

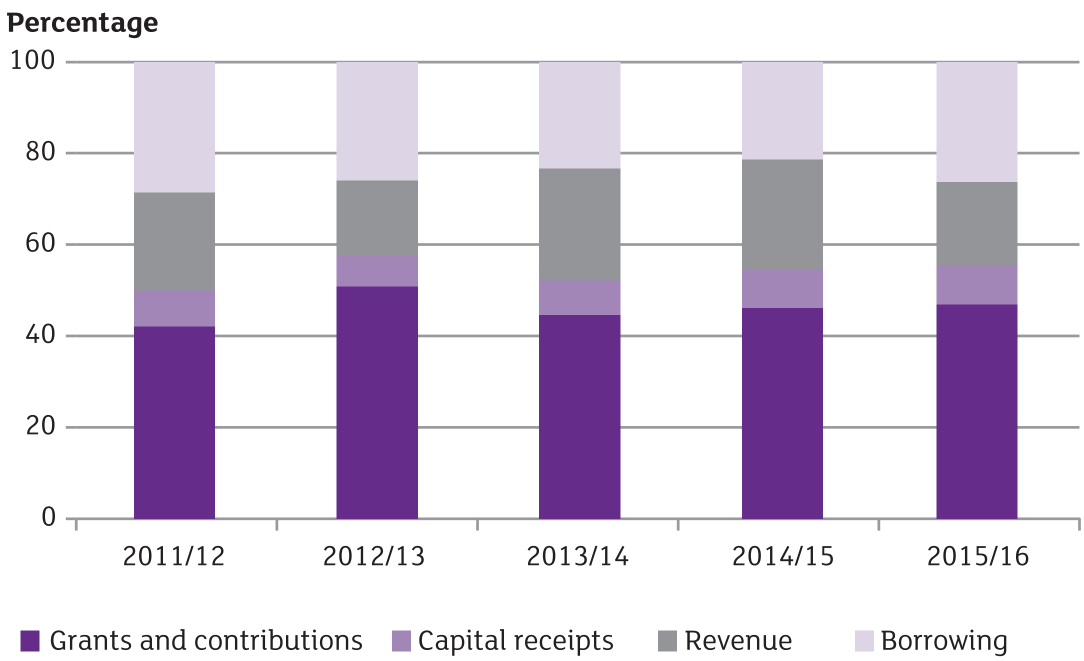
Councils finance capital spending in a number of ways, including:

- **the use of their own revenue funds** – councils are free to spend money from their revenue budgets on capital schemes; this is known as direct revenue financing. This includes the major repairs reserve which is a special reserve that provides capital funding for housing

- **capital receipts** – this is the money received from the disposal of capital assets and generally can only be used for repayment of debt or to finance new capital expenditure
- **borrowing** – councils can borrow money to pay for capital assets
- **grants and contributions** – these can come from central government or other organisations.

The following graph shows the proportion of capital expenditure financed by borrowing and other sources of finance in England and Wales over the period 2011/12 to 2015/16.

Financing local authority capital expenditure – England and Wales 2011/12 to 2015/16



Note: The 2011/12 figures exclude the housing self-financing transaction of approximately £13bn in order to avoid distorting the year-on-year comparisons.

Sources: National Statistics, Local Authority Capital Expenditure and Receipts, England: 2015/16 Final Outturn, September 2016; Welsh Government Statistical Release, Local Authority Revenue and Capital Outturn Expenditure: 2015/16, October 2016

The graph shows that the proportions of capital expenditure financed by:

- **grants and contributions** have risen over the years reflecting that all support from central government in England now comes through grants rather than the previous supported borrowing. In 2015/16 46% of capital expenditure was financed from grants and contributions
- **capital receipts** have remained a broadly stable proportion of financing at just under 10%. In 2015/16 9% of capital expenditure was finance from capital receipts
- **revenue** contributions accounted for 20% of the total in 2015/16
- **borrowing** fell from 29% in 2011/12 to 20% in 2014/15. This partly reflects a transfer of government funding in England to grant from support for borrowing but is also reflective of concerns over the long-term affordability of borrowing when councils are facing continuing pressure to reduce the revenue budgets used to finance borrowing.

THE PRUDENTIAL CODE

Before 2004, there was a very complicated framework of rules and regulations that controlled how councils were allowed to invest in assets and the amount that they could spend. April 2004 saw the introduction of CIPFA's Prudential Code for Capital Finance in Local Authorities. The Prudential Code provides a framework within which councils can judge for themselves whether capital investment is affordable, prudent and sustainable in the year in question and in future years. The Prudential Code is given statutory backing, which means that councils are required to 'have regard' to it, by the Local Government Act 2003 (in England and Wales) and the Local Government in Scotland Act 2003.

The current Prudential Code requires a council to think about six things when it agrees its capital programme:

- **The council's service objectives** – are the capital spending plans consistent with the council's strategic plan and its future plans for its services?
- **The stewardship of the council's assets** – is the capital expenditure being spent on new assets at the cost of maintaining existing assets?
- **The value for money offered by the plans** – have all the options for investment been considered and do the benefits outweigh the cost?
- **The prudence and sustainability of its plans** – can the council afford the borrowing now and in the future?
- **The affordability of its plans** – what are the implications for the council tax?
- **The practicality of the capital expenditure plan** – does the council have the resources to manage the project and does the total capital programme look sensible?

Councils need to prove that they are complying with the Prudential Code and this is done through a series of prudential indicators that are set locally and approved at the same time as the council sets its budget for the following year. The table below sets out the current key prudential indicators, but these will be changing at the end of 2017 following a review by CIPFA to ensure that they reflect the current pressures of local authorities.

Key prudential indicators

Indicator	Description
Estimate of the ratio of the capital financing costs to the authority's net revenue stream over the next three years	This indicator helps a council identify if borrowing costs become too high as a proportion of its budget. This is important as borrowing costs always have to be paid and are very hard to cut if resources fall.
Actual ratio of the capital financing costs to the authority's net revenue stream	The current value of the indicator above. This gives a baseline against which a council can see if borrowing is forecast to become a greater or a lesser part of the budget in the future. It also allows the accuracy of past estimates to be measured.
Estimates of the incremental impact of the capital investment decisions on the council tax for three years, or longer	Because all councils' borrowing is secured against future income including the council tax, ultimately all borrowing would have to be collected from council tax payers if no other income was available. It is therefore important to understand the impact of decisions on future council tax.
Authorised limit	The maximum amount of money a council can borrow. This amount can be changed at any point during the year by a meeting of the full council.
Operational limit	The maximum amount of money a council expects to borrow during the year. This is lower than the authorised limit and acts as a useful warning sign if it is breached during the year, which could mean that underlying spending may be higher or income lower than budgeted.
Debt compared to the capital financing requirement	Councils are only allowed to borrow money in the medium term to finance capital expenditure. Short-term borrowing can fund cash flows but borrowing cannot be used to fund the revenue budget. This indicator compares debt to the council's underlying need to borrow (its capital financing requirement) in order to show that borrowing is only being used to finance capital expenditure over the medium term.

In addition to setting limits for borrowing and the capital programme, the council is required to confirm that it complies with CIPFA's Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes. These require the council to set detailed ratios and limits for how it manages its borrowings and investments.

TREASURY MANAGEMENT

Treasury management is the term used to describe the way a council manages the cash it needs to meet both its day-to-day running costs and borrowing for capital expenditure. The following table highlights some of the main cash inflows and outflows of a council.

Key cash flows for a council

Day to day		Longer term	
Cash in	**Cash out**	**Cash in**	**Cash out**
Council tax and business rate income (or precept for upper-tier authorities) Revenue Support Grant Other grants and income from charging for services	Precepts (from billing authorities to precepting authorities) Wages and salaries Payments to suppliers Grants to other bodies	Cash-backed reserves and provisions Capital receipts Grants and contributions Borrowing	Capital expenditure Repayment of borrowing

The treasury management function for a council will make the arrangements to borrow and invest money over either the short term or the longer term in order to ensure that it has money available when it needs it. Councils may borrow money from banks and building societies, other councils, the financial markets or the Public Works Loan Board (PWLB), which is part of the government's Debt Management Office and allows councils to borrow at interest rates closer to those paid by central government for its borrowing. Councils invest money mainly with banks and building societies but may also invest in other places such as money market funds and the government's Debt Management Office. The government intends to simplify the institutional arrangements by abolishing the PWLB and transferring its powers to HM Treasury, which in turn will delegate operational responsibility to the Debt Management Office. These changes will have no practical implications for local authorities.

In making arrangements for treasury management, a council is required to follow CIPFA's Treasury Management Code. The Code aims to help ensure that councils manage the significant risks associated with the function while also ensuring the council receives value for money. It defines treasury management as:

…the management of the organisation's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.

It is very important that councils understand the risks that are associated with treasury management, as highlighted by the collapse of the Icelandic banks a number of years ago, which put at risk substantial funds that had been invested by councils. The key treasury management risks are:

- **credit risk** – the risk that a bank or other institution will not be able to pay back the money invested in it
- **interest rate risk** – the risk that a council's budget will be adversely affected by unforeseen changes in interest rates
- **liquidity risk** – the risk that a council will have funds tied up in long-term investments when it needs to use that money
- **refinancing risk** – the risk that when loans and investments reach the end of their term, the council will not be able to re-borrow or reinvest the money on acceptable terms or interest rates
- **legal and regulatory risk** – the risk that unforeseen legal and regulatory changes have an adverse impact on a council.

A council is required to approve a treasury management strategy, which sets out how it will borrow and invest money and manage those risks. The strategy is likely to include the following items:

- details of its appetite for risk and how it proposes to manage its risks, ensuring the key principles of security (getting your money back) and liquidity (having money available when you need it); and only when these two principles are ensured, considering yield (how much return it gets for its investment)
- details of how it assesses the credit worthiness of institutions it is planning on investing money with
- details of its training plans for both officers and members
- details of its use of third parties such as treasury management advisors.

It should also include the following treasury management indicators:

- An upper limit on the level of investments for longer than 364 days, which limits the amount of money that a council can invest for a fixed term of a year or more to ensure that the liquidity risk is managed. Longer-term investments also increase credit risk as councils may not be able to get their money back, or may face heavy penalties if they can do so, if an institution's credit worthiness changes. When the Icelandic banks' credit ratings were downgraded, many councils were unable to take existing investments out of these banks.
- Upper limits for fixed interest rate and variable interest rate exposures, which set the maximum percentage of total borrowings with fixed rate loans and the maximum percentage with variable rate loans. This helps councils manage their interest rate risks and exposure to adverse changes in interest rates.
- Upper and lower limits for the maturity structure of borrowings. The maturity structure of borrowings is a term used to describe the profile of the dates that loans need to be repaid. A council will want to arrange its portfolio of loans so that they all do not come to an end at the same time and so that at any time it is borrowing only the amount of money it needs. This indicator helps a council

manage its refinancing risk and avoid unnecessary credit risk by having to invest money as a result of over-borrowing.

The way the treasury management risks interact is very complicated and councils will rely heavily on professional advice from specialist officers and external advisors. It is important, however, that senior officers and councillors understand the treasury management risks the council is taking and they should remember that the responsibility for treasury management must always remain within the council.

PRUDENTIAL CODE AND TREASURY MANAGEMENT CODE CONSULTATIONS

The Prudential Code and the Treasury Management Code were last updated in 2011. Since then the landscape for local government has changed significantly following the sustained period of reduced public spending and the developing localism agenda. In spring 2017, CIPFA considered it an appropriate time for both Codes to be reviewed and sought views from stakeholders as to areas where the Codes could be strengthened or amended. Further consultations on the proposed changes were issued in the summer of 2017, with the revised Codes possibly to be published in time for implementation in 2018/19.

CHAPTER FOUR

Local authority accounting and reporting

Local authority accounting differs from private sector accounting in a number of important ways. Although local authority accounting is based on the same accounting standards, since these are mainly designed for the private sector in some cases they need to be adapted or interpreted for councils to use. In addition, the government makes specific rules known as statutory requirements that local authorities must follow when they prepare their financial statements, limiting the amount that can be charged to council tax payers and avoiding significant changes in expenditure from one year to the next. As a result, local authority accounting is a combination of the accounting standards that dictate how all organisations should account, and legislation.

Accounting standards are set by the International Federation of Accountants (IFAC) and are known as International Financial Reporting Standards (IFRS). These set out how accountants should present items in the annual statement of accounts. Legislation is set out through a mixture of regulations and accounting directions that are issued by the Department for Communities and Local Government (DCLG), requiring councils to treat certain items in the accounts differently to the accounting standards.

All the accounting requirements for councils are brought together in CIPFA's Code of Practice on Local Authority Accounting in the United Kingdom. This chapter of the guide outlines some of the key accounting principles and looks at the annual statement of accounts that all councils are required to produce. This is a simplified overview that is aimed at giving the reader a general understanding when reading the accounts of councils.

ANNUAL STATEMENT OF ACCOUNTS

Each local council is required to produce an annual statement of accounts by 30 June immediately following the end of the financial year. This deadline is changing to 31 May for accounts produced in respect of the financial year 2017/18 and future years. The accounts contain detailed information on the financial position of the council. They show not just the income and expenditure of the council, but also the assets and liabilities it holds. The statement of accounts is a key way that councils are able to demonstrate that they are using public money properly, known as financial stewardship. The format of the statement of accounts is set out in the *Code of Practice on Local Authority Accounting in the United Kingdom* and contains the following key statements.

Comprehensive income and expenditure statement	This is where all the income and expenditure of the council is recorded in line with accounting rules. This statement is similar to the one you would find in a private company.
Movement in reserves statement	This statement shows the impact of the financial year on the council's reserves. This statement also includes all of the income and expenditure that is recognised under accounting rules but which is then adjusted by legislation to give the amount of expenditure that has been funded by the local tax payer.
Balance sheet	This statement summarises a council's financial position at each year end and reports the assets, liabilities and reserves of the council. Some of the reserves are specific to councils, such as the pensions reserve and the capital adjustment account, and exist to allow accounting entries required by legislation.
Cash flow statement	This summarises the cash flows that have been made into and out of the council's bank account during the financial year.

ACCRUALS

The principle of accruals is a key one for accounting and it describes when income and expenditure is recognised (included) in the accounts. This contrasts with the simplest form of accounting, the cash basis, when transactions are recognised in the accounts when the actual cash is received or paid out. This cash basis would not, however, accurately reflect the true position of the council as it would not show how much the council owes or is owed.

Under the accruals basis of accounting, income and expenses are recorded when earned and incurred, regardless of when cash is exchanged (ie received or paid). Income is recognised when it is earned (ie services are provided) and expenses are recognised when costs have been incurred (ie goods or services are provided).

Take for example a council purchasing home care services from a supplier in order to meet the needs of an elderly resident who pays for the service received. The council would include the cost of the home care service in its accounts when it is provided even if it had not yet been invoiced or paid for. It would then also include the income due from the resident as soon as the service was provided. Income and expenses included in a council's accounts that have not yet been settled (ie cash has not been received or paid) will give rise to debtor (receivables) and creditor (payables) balances in the council's balance sheet. In summary:

- **Debtors/receivables** come into existence where income has been recognised but payment has not yet been received by the council. Put simply, debtors are individuals or organisations that owe the council money.
- **Creditors/payables** come into existence where expenditure has been recognised but payment has yet to be made by the authority. Put simply, creditors are individuals or organisations to whom the council owes money.

Taking the home care example, the debtor would be created and the income recognised even where the income is payable many years in the future following the eventual sale of the client's home.

CAPITAL ACCOUNTING

Capital accounting is the term used to describe the entries in a council's accounts that are made in relation to its non-current assets, otherwise known as property, plant and equipment – mainly buildings, infrastructure and pieces of equipment. They are called 'non-current' as they are expected to provide services or economic benefit to the council for more than one year. There are two key elements to capital accounting:

- to ensure that the value of the council's assets are correctly reflected in its balance sheet so that the balance sheet gives an accurate view of the council's overall financial position
- to reflect the cost of using assets as an expense of the council so that the cost of service provision shows the total cost.

ASSET VALUATION

When the council invests in new assets it includes these in the balance sheet at the cost of the investment made plus any expenses. In order to ensure that the balance sheet is kept up to date, assets need to be regularly revalued, at least every five years or more frequently for the assets whose values may be volatile. If council assets are not regularly updated, then the balance sheet will very soon become out of date. To take an extreme example, if a Victorian school building were left on the balance sheet at the amount it cost to build, it may be undervalued by several tens of millions of pounds. The following table sets out the main categories of assets and how they are valued.

The table reflects the Code's adoption of IFRS 13 Fair Value Measurement, which applied from 1 April 2015. However, the Code adapts the measurement requirements for property, plant and equipment and has introduced the concept of current value. This definition of current value means that the measurement requirements for property, plant and equipment providing service potential for an authority have not changed from previously, ie they are measured for their service potential either at existing use value, existing use value – social housing (for council dwellings) or depreciated replacement cost (for specialised assets), and not at fair value. Since 2015/16, the Code has however changed the measurement requirements for assets classified as surplus assets. These assets are now measured at fair value in accordance with the definition in IFRS 13 and without any adaptations to that definition. Where applicable, all other assets are measured at fair value.

Category of asset	Description	Valuation	Description
Land and buildings	Land and buildings used to provide services	Current value based on existing use or depreciated replacement cost	A valuation based on how much the assets could be sold for if they were sold for the same purpose they are currently used for, eg a school is valued if sold for use as a school rather than for housing. Revalued at least every five years and more frequently if necessary.
Vehicles, plant and equipment	Vehicles, plant and equipment used to provide services		
Infrastructure	For example roads, footpaths, bridges and tunnels	Depreciated historical cost	The cost of acquiring the asset or work carried out to date.
Assets under construction	New buildings that are in the process of being built	Cost	
Housing – dwellings	Houses used to provide social housing	Existing use value – social housing	The current value of the houses if they were to be sold to be used for letting for social rents.
Heritage assets	An asset with special qualities that is held and maintained principally for its contribution to knowledge and culture	Valuation, or cost where a value is not available	Value does not have to be professional valuation but could be an insurance valuation (for museum or art gallery exhibits, for example). For some assets, a value may not be available (for example an archaeological site) and cost can be used where this is available.

Category of asset	Description	Valuation	Description
Community assets	Assets that the council intends to hold in perpetuity, for example a park	Cost or as per heritage assets	Councils can choose to use cost or the same basis as heritage assets.
Investment assets	Assets held for income generation purposes rather than service provision	Fair value as at balance sheet date	These are valued at fair value (ie highest and best use).

Where a council is in the process of selling an asset or has made the decision to sell an asset, it is classified as an asset held for sale and is included in current assets on the council's balance sheet. This reflects the fact that the council does not intend to hold the asset for the long term.

When an asset is revalued, this creates a difference between its previous value and its current value. A change in valuation is generally reflected in the revaluation reserve. When an asset's value falls, ie a revaluation loss (or it is impaired eg becomes obsolete or physically damaged), the revaluation reserve can be reduced by this fall in value provided that the value of the asset in question has previously increased by at least as much (accumulated revaluation). If the accumulated revaluation figure for an asset is not enough, any balance between the fall in value and the accumulated depreciation has to be charged to the comprehensive income and expenditure statement.

DEPRECIATION

Depreciation is the term used to describe the charge that is made to the comprehensive income and expenditure statement to reflect the council's use of its assets. The argument is that, in using an asset to provide services, its value is diminished. This is most simply illustrated by taking a vehicle as an example. Suppose a council buys a new minibus for £20,000 which it intends to use for ten years, at which point it expects to sell it for £10,000. If it included just the cash values in its accounts, it would have expenditure of £20,000 in the first year and income of £10,000 in year 11. In years two to ten it would still be using the minibus but would show no cost in its accounts of doing so. If, instead, it spread the £10,000 cost of owning the asset (the purchase cost of £20,000 less its final value of £10,000) over the ten years of expected use, it would charge £1,000 per year to its comprehensive income and expenditure statement.

The actual calculation of depreciation is slightly more complicated in practice but the principle remains the same, with an asset's value, less any final value on disposal, being spread over the expected life of the asset. As the value of land, provided it is not being used for landfill or mineral extraction, does not change as a result of using it, land is not depreciated – only the buildings upon it.

Capital Accounting in the Movement in Reserves Statement

The comprehensive income and expenditure statement for a council will include the costs of depreciation, charges for impairment and gains and losses on the disposal of non-current assets. Depreciation and impairment have been described above while gains and losses on the disposal of non-current assets reflect the difference between the balance sheet value of an asset and the amount for which it is sold. Due to the way councils are financed and the fact that money received for the sale of non-current assets is tied up in capital receipts, the government does not want these to impact councils' revenue reserves. So regulations have been made to take these items out in the movement in reserves statement. Depreciation is replaced with a minimum revenue provision, which makes a charge to the accounts for the repayment of borrowing associated with capital expenditure. These adjustments are made against the capital adjustment account, which is an unusable reserve and is one of the reserves specific to councils' accounts.

RESERVES AND PROVISIONS

Reserves

Reserves are split into usable reserves and unusable reserves in the balance sheet. Usable reserves include general and earmarked reserves, ie those reserves that can be spent on future services. Unusable reserves include all those accounting reserves that cannot be used for expenditure on services (these are explained further below).

General and Earmarked Reserves

When reviewing their medium-term financial plans and preparing their annual budgets, councils should consider the establishment and maintenance of reserves. These can be held for three main purposes:

- a working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – this forms part of general reserves
- a contingency to cushion the impact of unexpected events or emergencies – this also forms part of general reserves
- a means of building up funds, often referred to as earmarked reserves, to meet known or predicted requirements, but where the requirements or amounts are not certain enough to create a provision.

Earmarked reserves formally remain part of the general fund of the council. The general fund of a council represents the money available to local tax payers that can be used for expenditure on services. Key categories of earmarked reserves are as follows.

Category of earmarked reserve	Rationale
Sums set aside for major schemes, or to fund major reorganisations	Where major expenditure is planned in future years, it is prudent to set aside resources in advance.
Insurance reserves	Reserves held to fund repairs or replacement of assets where the council chooses not to buy insurance against these costs with external insurance companies.
Reserves of trading and business units	Surpluses arising from trading or business units may be held back to cover potential losses in future years, or to finance capital expenditure.
Reserves retained for service departmental use	Councils may let departments keep all or some of any underspends to use for future projects.
Reserves for unspent revenue grants	Where revenue grants are received by the council with no conditions or where the conditions are met and expenditure has yet to take place, it is recommended that these sums are held in earmarked reserves. (For further information on grant conditions please refer to Module 2, section C of the 2016/17 Code Guidance Notes.)
Schools balances	These are the unspent balances of individual schools' budgets that can only be used by those schools.

Unusable Reserves

Councils also show a number of accounting reserves on their balance sheets. These are not backed by cash so cannot be spent on council services but arise because of entries in the accounts. These reserves are as follows.

Category of unusable reserve	Rationale
Pensions reserve	This reflects the difference between the amount charged for pensions in the accounts under accounting rules and the actual payments made to various statutory pension schemes for the year.
Revaluation reserve	The accumulated balance of changes in the value of non-current assets.
Capital adjustment account	The difference between depreciation and the charges made to the accounts under capital accounting rules and the amounts charged under legislation.
Available for sale financial instruments reserve and financial instruments adjustment account	The difference between the amounts charged to the accounts for local authority borrowings and investments under accounting rules and the amounts charged under legislation.
Unequal pay back pay account	The difference between the amounts charged to the accounts for compensation for unequal pay under accounting rules and the amounts charged under legislation.
Collection fund adjustment account	The difference between the amounts recognised in the accounts for council tax and non-domestic rates income (England) and the amounts charged under legislation.

Other Reserves

Councils will hold the following two usable reserves:

- **capital receipts reserve** – this reserve holds the proceeds from the sale of assets, and can only be used to fund capital expenditure or repay debt
- **major repairs reserve**, where relevant (this applies only to housing authorities in England and Wales) – in England this reserve records the unspent amount of HRA balances for capital financing purposes in accordance with statutory requirements. In Wales this represents the amounts unspent from the major repairs allowance capital grant.

Provisions

A council may set up a provision when it knows that it is highly likely that it will have to pay out money or transfer assets in the future; for example, the council may be involved in a court case that could eventually result in the payment of compensation. Provisions are charged to the appropriate service line in the comprehensive income and expenditure statement when the council becomes aware of the need for them. When payments are eventually made, they are charged to the provision carried in the balance sheet. The level of provisions should be regularly reviewed to ensure they reflect the most accurate estimate of future cost.

PENSIONS

IAS 19 Employee Benefits is probably one of the best known financial reporting standards as it has been frequently mentioned in news items about final salary pension schemes. The accounting standard requires the balance sheet to reflect a snapshot of a pension fund's assets and liabilities at the end of the financial year and the associated costs to be reflected in the comprehensive income and expenditure statement.

The standard applies to all employee benefits but has a particular impact on defined benefit schemes where the pension paid is based upon the salary of the recipient, not the amount they have paid into their pension pot. Police and fire schemes are excluded from the accounting standard as they are 'unfunded' schemes where contributions are used to pay existing pensions with the difference underwritten by government.

The difference between the cost of pensions under accounting rules (IAS 19) and the actual payments made is reversed out of the accounts in the movement in reserves statement against the pensions reserve.

OTHER ACCOUNTS

Councils may use other accounts to record income and expenditure relating to certain services they provide or functions they carry out. Key accounts include:

Trading accounts	Used where a council has set up a trading arm to record income and expenditure to assess whether or not the trading arm is creating a surplus of income over expenditure. The word 'surplus' is used instead of 'profit' in not-for-profit organisations such as councils.
Housing revenue account	Used to record the income and expenditure related to a council's housing function and required by legislation.
Collection fund	Used to record income and expenditure related to council tax and non-domestic rates collected by billing authorities.

LOCAL AUTHORITY FINANCIAL REPORTING

The statement of accounts is a key way that councils are able to show they are using public money properly and forms the core of local authority reporting. In addition, councils have to comply with some other key aspects of financial reporting.

Narrative Reporting

The financial statements on their own can be difficult for a lay person to understand and interpret, so explanations and commentary are needed to help the reader make sense of the financial statements and to help demonstrate the extent to which the objectives of the council have been achieved.

Remuneration of Senior Officials

Since 31 March 2010, councils have been required to include detailed remuneration information for their senior employees in their annual statement of accounts. Remuneration includes all monetary and nonmonetary payments made to an employee as part of their employment. It does not include employer pension contributions. However, for the purposes of disclosing senior officer remuneration in England and Wales, employers' pension contributions must be reported in addition to the remuneration.

The Transparency Agenda

Councils are required to publish details of all items of expenditure over £500 because the government wants to encourage 'armchair auditors' – members of the public with an interest in council finances who are prepared to question councils over what they spend. In February 2015, the DCLG published its latest version of the Local Government Transparency Code, which councils are required to follow.

The code requires councils to publish the following data:

- expenditure over £500
- Government Procurement Card transactions
- procurement information about every invitation to tender for contracts that exceed £5,000 and details of any contracts, commissioned activity, purchase order, framework agreement and any other legally enforceable agreement in relation to the provision of goods and/or services with a value that exceeds £5,000
- information on public land and buildings
- information on social housing asset value (details on the value of social housing assets within local authorities' housing revenue accounts)
- grants to voluntary, community and social enterprise organisations
- an organisational chart of the staff structure of the council including salary bands and details of currently vacant posts
- information on trade union facility time including the number of staff who are union representatives, the number of staff who devote at least 50% of their time to union duties and the names of the trade unions represented

- income and expenditure on the authority's parking account including details of revenue collected from on-street parking, off-street parking and penalty charge notices and an analysis of how any surplus on the parking account has been spent
- information on parking spaces including the number of marked out controlled on and off-street parking spaces within their area
- information on senior employee salaries
- information on the council's constitution
- the 'pay multiple' – the ratio between the highest paid salary and the median average salary of the whole of the council's workforce
- information about the council's counter fraud work and the measures in place to combat fraud.

This data should be published on the council's website and in a format that is as widely usable as possible.

CHAPTER FIVE

Governance and the role of the chief financial officer

GOVERNANCE

Governance comprises the arrangements[1] put in place to ensure that the intended outcomes for stakeholders are defined and achieved.

Source: *International Framework: Good Governance in the Public Sector*, IFAC/CIPFA, 2014

Key elements of the systems and processes that comprise a council's governance include arrangements for:

- developing codes of conduct, which define standards of behaviour for members and staff
- ensuring compliance with relevant laws and regulations, and internal policies and procedures, and that expenditure is lawful
- documenting a commitment to openness and acting in the public interest
- establishing clear channels of communications with all stakeholders
- developing and communicating the authority's objectives and intended outcomes
- reviewing the effectiveness of the authority's decision-making framework, including delegation arrangements and decision-making in partnerships
- measuring the performance of services for users, for ensuring they are delivered in accordance with the authority's objectives and that they represent value for money

1. Includes political, economic, social, environmental, legal and administrative structures and processes and other arrangements.

- defining the roles and responsibilities of the executive, non-executive, scrutiny and officer functions
- reviewing the effectiveness of the framework for identifying and managing risks and demonstrating clear accountability and for ensuring effective counter-fraud and anti-corruption arrangements are developed and maintained.

Each council is required to include an annual governance statement with its statement of accounts that sets out how the council has monitored its governance arrangements throughout the year and reviewed how effective they are in supporting planned outcomes.

CIPFA has worked with the Society of Local Authority Chief Executives and Senior Managers (Solace) to produce the CIPFA/Solace Framework Delivering Good Governance in Local Government and accompanying guidance, which helps councils ensure that their governance arrangements meet best practice. New editions of the framework and guidance were published in 2016.

THE ROLE OF THE CHIEF FINANCIAL OFFICER

The chief financial officer (CFO) is the person in the most senior finance role in a council. The CFO in a council has to be a member of a professional accountancy body such as CIPFA. This means that in carrying out their job they are bound by very rigorous professional rules and expectations. The CFO also has very specific legal responsibilities to the local tax payer.

The role and responsibilities of the 'treasurer' were developed by case law in England and Wales. In Attorney General v De Winton 1906, it was established that the treasurer is not merely a servant of the council, but holds a fiduciary responsibility to local tax payers. This means that when CFOs give advice and carry out their jobs they have to think about what is the best decision not only for the council, but also for local tax payers.

Section 151 of the Local Government Act 1972 requires councils to "make arrangements for the proper administration of their financial affairs" and appoint a CFO to have responsibility for those arrangements.

This means that the CFO is legally responsible for ensuring that a council manages its finances properly.

To help CFOs to do their job and councils to understand how they can ensure their arrangements support CFOs in their legal responsibilities, CIPFA has published its Statement on the Role of the Chief Financial Officer in Local Government (2016), plus a separate statement for police, recognising their different arrangements. The statement goes into detail about the role, but it is based upon the five principles set out below.

The CFO in a local authority:

- is a key member of the leadership team, helping it to develop and implement strategy and to resource and deliver the authority's strategic objectives sustainably and in the public interest
- must be actively involved in, and able to bring influence to bear on, all material business decisions to ensure immediate and longer-term implications, opportunities and risks are fully considered, and alignment with the authority's financial strategy
- must lead the promotion and delivery by the whole authority of good financial management so that public money is safeguarded at all times and used appropriately, economically, efficiently and effectively.

To deliver these responsibilities, the CFO:

- must lead and direct a finance function that is resourced to be fit for purpose
- must be professionally qualified and suitably experienced.

CHAPTER SIX

Audit and value for money

EXTERNAL AUDIT – CURRENT ARRANGEMENTS

The external auditor of a private sector organisation is required to carry out an in-depth examination of the annual statement of accounts and certify that it represents a 'true and fair' view of the financial position of the organisation. If an auditor finds material errors in the accounts or views them as misleading, they can 'qualify' them, which means that they publicly report on why accounts do not give a true and fair view.

This is essentially the same process that is carried out by the external auditor of a council. However, external audit is also very important in ensuring proper stewardship of public money; therefore, in councils, external auditors look not only at the financial statements but also at the financial aspects of how a council is managed. The external auditor must satisfy themselves that the accounts are prepared in accordance with regulations and accounting rules and that the council made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. Auditors may report on their work to the general public and other key stakeholders.

In England, until 31 March 2015, the Audit Commission was responsible for appointing local authority auditors from private firms of accountants. However, the Local Audit and Accountability Act 2014 formally abolished the Audit Commission and established new arrangements for the audit and accountability of certain public bodies including local authorities. Importantly, it requires these public bodies to appoint their own external auditors, replacing the previous process of commissioning of external auditors that had been carried out by the Audit Commission. A transitional body is overseeing the existing contracts in the remaining time that they have to run.

Smaller councils, such as parish or town councils, are able to appoint their own auditors for the financial year beginning 1 April 2017 and larger authorities, such as London boroughs, county councils or unitary authorities, are required to appoint their own auditors to start from the financial year beginning 1 April 2018. Many have done this by employing a company, Public Sector Audit Appointments Limited (PSAA), set up by the local government sector to manage auditor appointments on behalf of local authorities.

In Wales, audit is the responsibility of the Wales Audit Office, which carries out audits using its own staff.

The Code of Audit Practice, published and maintained by the National Audit Office, sets out in detail how the auditor should fulfil this role and gives further details of the external auditor's objectives when conducting an independent assessment of a council. The *Code of Audit Practice* has to be approved by both Houses of Parliament at five-yearly intervals and auditors must comply with it. The most recent version applies from 1 April 2015. In Wales, the *Code of Audit Practice* is the responsibility of the Wales Audit Office and is approved by the Welsh Assembly.

The *Code of Audit Practice* also outlines how auditors should fulfil other statutory functions outlined in the Local Audit and Accountability Act 2014. These functions are:

- to give electors the opportunity to raise questions about the accounts and then to consider and decide upon any objections received from electors in relation to the accounts
- to apply to the court for a declaration that an item of account is contrary to law
- to consider whether to issue an advisory notice or to make an application for judicial review.

The results of audit work are communicated in the following reports:

- the audit planning document – this sets out how auditors intend to carry out their responsibilities, in the light of their assessment of risks
- reports to councillors or officers on specific areas of their audit work where they have concerns; these can be in writing or verbal

- an audit report, including the auditor's opinion on the financial statements; a conclusion about whether the audited body has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources; and a statement on the consistency of consolidation schedules prepared by the authority with the financial statements
- a certificate that the audit of the accounts has been completed in accordance with statutory requirements
- an annual audit letter about the key issues that the auditor considers should be brought to the attention of the audited body.

Other specific reports may be issued at any point during the audit process, if required:

- to consider whether, in the public interest, an issue should be considered by the body concerned or brought to the attention of the public
- to make written recommendations that need to be considered and responded to publicly.

The external auditor has particular duties in relation to questions of:

- legality – whether the council has incurred expenditure that it had no legal power to do
- rights of challenge to the accounts – where an elector has formally raised an issue with the auditor about an item in the accounts.

To fulfil these duties, the auditor has access to all documents as appear necessary for the purposes of the audit. Auditors may decide:

- to refer any issues to the council, so that the council can formally and publicly consider their recommendations, or
- to take the matter through the courts, so that expenditure can be stopped, or
- to ask the courts to review a decision the council has made. This is known as judicial review.

Before each audit of the financial statements, the current requirement is that accounts and documents must be available for public inspection for 30 working days. Any person interested may come into the council to view those accounts and supporting documents. They are allowed to make copies. In addition, those entitled to vote in an area may meet the external auditor and question them about the accounts.

INTERNAL AUDIT

The internal audit team may be employed directly by a council or by an external service provider. All councils are required by legislation to have internal audit to evaluate the effectiveness of their risk management control and governance processes. This function must be performed to professional internal audit standards.

The Public Sector Internal Audit Standards define internal auditing as follows:

Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

In order to carry out their work, internal auditors will focus their efforts on major areas of risk, including strategic and service risks as well as financial risks. The audit could include a range of activities such as:

- reviewing the procedures for spending money and collecting income within the council and testing transactions
- reviewing the quality and accuracy of performance data and management reports
- reviewing compliance with council policies and legislation
- providing assurance on the effectiveness of arrangements put in place to achieve the council's goals.

The head of internal audit is required to give an annual opinion on the governance, risk management and the internal controls within the council. They may also provide support for other functions such as counter fraud and corruption, helping share anti-fraud and anti-corruption messages with the employees of the council.

The role of internal audit is set out in a written document, known as the charter, which also ensures it has access to all the council's systems, records and personnel that it needs to do its job properly. This charter also sets out internal audit's power to report its findings to ensure that it has appropriate access to decision-making bodies.

AUDIT COMMITTEES

Audit committees are special committees of the council that are set up to provide an independent and high level resource to support good governance and strong public financial management. They play an important role in the oversight of both internal and external audit. Audit committees often include independent members who are not councillors but sit on the committee for their financial knowledge. The head of internal audit and the external auditor should have a right of direct access to the audit committee.

CHAPTER SEVEN

Education

INTRODUCTION

The local authority role in education is carried out by county, metropolitan and unitary councils. In London, the London boroughs have responsibility for education, while the mayor has a role in promoting educational standards across London.

Education is provided in England by the main types of school described below:

- Schools which are maintained by and funded through local councils. This includes community schools, voluntary controlled schools, voluntary aided schools and foundation schools.
- Academies, which are publicly funded independent schools. They are funded directly by the government through the Education & Skills Funding Agency (ESFA), although their funding is calculated on a comparable basis to that received by local authority maintained schools in the area in which the academy is situated. Academies have more freedom to decide how they operate and can also have involvement from private sector companies and sponsors.
- Free schools, which are very similar to academies in the way they are funded and in their freedom to decide how they will operate. They are often established in response to groups of local parents getting together to decide that there is a need for a new school in their area. They don't have to follow the national curriculum. Free schools include:
  - university technical colleges (UTCs), a type of secondary school for those aged 14–18, in England, led by a sponsor university. In January 2017, there were 48 UTCs
  - studio schools, which are designed for 14- to 19-year-olds of all abilities. They are small schools for 300 students, with year-round opening and a 9–5 working day. They are said to

feel more like a workplace than a school. In January 2017, there were 36 studio schools.

Local authorities must ensure that there are sufficient good quality school places in their locality. They have a key role in ensuring that the schools admission process is fair and at present still have an important role in the provision of school places. In January 2017[2] there were:

- 16,786[3] state funded primary schools (excluding special academies and alternative provision) of which 13,038 were funded by local authorities
- 3,408 state funded secondary schools including 1,083 funded by local authorities.

In January 2017, approximately 3.5m (76%) primary school pupils and 1.0m (31%) secondary school pupils were educated in the local authority funded schools.

For councils, the main issue raised by schools converting to academy status is typically managing the change and minimising the impact on their finances, particularly where the level of services sold to schools changes if the new academies then choose to buy those services from elsewhere.

Education remains a key priority for the government and the Spending Review and Autumn Statement 2015 included a commitment to protect schools' funding in line with inflation.

Education remains the biggest local government service, with budgeted revenue expenditure of £34bn in England in 2016/17. This figure excludes expenditure on academies, which are funded directly by the Department for Education via the Education Funding Agency. Education accounted for around 31% of total spending on all local government services.

2. National Statistics – Schools, pupils and their characteristics: January 2017 (DfE).

3. Figures exclude special academies and alternative provision.

SCHOOLS FUNDING FORMULA

At present the funding of each school is determined by a national formula allocating grant to each local education authority and then a formula set by each local authority to allocate funds to each of its schools. The government started a process in 2012 to reform the school funding system to make it fairer, more consistent and more transparent. The government set out how the system would start to change ahead of the then anticipated introduction of a national funding formula by which the core funding of each school would be determined.

Currently, revenue funding is distributed to local authorities through the Dedicated Schools Grant (DSG) which is allocated to them on the basis of historic data. The DSG is split into three blocks: the schools block, special needs block and early years block. The schools block is intended to cover core provision for pupils in primary and secondary education to the age of 16.

Most of the DSG is distributed to maintained schools using locally determined formulae. However, there has been significant variation in how local authorities allocate funding to schools. In order to move to a more consistent, comparable and transparent system, from April 2013 local authorities were required to use much simpler formulae.

Local authorities are now limited to a maximum number of factors in their formulae, which relate largely to pupil characteristics and pupil numbers (taken from the Annual School Census data), and less so to the circumstances of the school. Funding is available for pupils with high needs in special schools or mainstream schools, based on the needs of the pupil. From 2014/15, the government required that a minimum of 80% of delegated schools block funding is allocated through an appropriate and locally determined combination of the pupil-led factors.

In March 2014 the government announced that it had decided not to set out a multi-year process of converging all local authorities towards a single funding formula at that time. Instead, the government published a consultation on fairer school funding from 2015. This proposed allocating additional funding of £350m for 2015/16 – every local authority would attract a minimum funding level for every pupil and school.

Approach for 2015/16 and 2016/17

Following the above consultation and the government's response, the DfE published Fairer Schools Funding: Arrangements for 2015 to 2016 in July 2014. This set out a number of reforms that the government was making to the schools funding system for 2015/16. The main proposals included:

- all local authorities to be funded to at least the same cash level as in 2014/15
- to allocate an additional £390m (rather than £350m announced earlier) to fund schools in the least fairly funded authorities.

To protect schools from significant budget reductions, the government ensured that no school saw a reduction larger than 1.5% per pupil in its 2014/15 budget compared to 2013/14 (excluding sixth form funding). This commitment was reiterated for 2015/16. In addition, local authorities with falling school numbers continued to be protected by arrangements that ensure that no authority lost more than 2% of its budget in cash terms.

For 2016/17, allocations for the schools block were calculated largely on the basis of how much an area received per pupil in 2015/16 with some adjustments. The £390m fairer schools funding was continued. The core schools' budget continued to be protected and per pupil funding together with the pupil premium was maintained in cash terms. However, the government made savings from the Education Services Grant (ESG) which funds local authorities and academies for services such as school improvement and education welfare services.

Once a school has converted to academy status, it ceases to be funded through the council. Instead, its funding comes in the form of a grant, known as the General Annual Grant, paid by the Education and Skills Funding Agency.

Consultation: Schools National Funding Formula

A key determinant of how much a local authority received per pupil in its schools block was how much it had received in previous years. Owing to historical differences in funding, the average amount per pupil funding varies considerably between authorities. Before the 2017 election the government was proposing the phased introduction of a new national funding formula from 2018/19 to address these variations, but the future of this proposal is now unclear.

PUPIL PREMIUM

The pupil premium aims to provide significant funding for disadvantaged children to help close the attainment gap. The pupil premium is allocated to schools for most pupils and can be seen separately in their funding. Schools can decide how the pupil premium is spent but they have to say how they have used the extra money to support deprived pupils.

For 2017/18, schools attract £1,320 for primary school pupils, £935 for secondary school pupils and £1,900 per looked after child. The pupil premium is allocated based on the number of children who are known to be eligible for free school meals and children who have been looked after (by the council) for more than six months.

SIXTH FORM AND FURTHER EDUCATION

The government is committed to helping all 16- and 17-year-olds to take part in education or training and raised the participation age to 18 in 2015.

Raising the participation age does not mean young people must stay in school; they will be able to choose one of the following options:

- full-time education, such as school, college or home education
- work-based learning, such as an apprenticeship
- part-time education or training if they are employed, self-employed or volunteering for more than 20 hours a week.

For this is to be successful, all sections of the education system will need to play their part. Councils are expected to play a key role in championing the needs of young people in their areas and in working with partners to achieve full participation.

EDUCATION IN WALES

In Wales there are some 1,574 state schools, with around 466,555 pupils. In January 2016 there were 13 nursery, 1,310 primary, 205 secondary, seven middle and 39 special schools. Secondary school education is provided through community-based comprehensive schools. Overall, there were 21 fewer schools than in 2015.

Education is the biggest local government service in Wales, with budgeted revenue expenditure of £2.5bn in 2016/17 accounting for 33% of total budgeted expenditure.

The Welsh Government provides funding to local authorities for pre-16 provision in schools through the local government revenue settlement. Local authorities are responsible for the planning, organising and funding of maintained schools in their area according to local needs and priorities.

Local authorities set budgets for schools according to a local formula and in accordance with the School Funding (Wales) Regulations 2010. The regulations require that 70% of funding for individual schools' budgets is distributed according to factors which are learner led. Local authorities must consult their schools forum prior to setting schools' budgets.

Post-16 Education in Wales

The Welsh Government funds individual further education institutions and local authorities for maintained school sixth form provision. Grant agreements between the government and the institution set out the funds that the government has agreed to pay for post-16 learning, how the funds will be paid and the terms and conditions for the use of funding. This includes monitoring and audit requirements for the use of funds.

In February 2011, the Minister for Education and Skills announced a comprehensive review of post-16 planning and funding. A new post-16 planning and funding framework was introduced for the 2014/15 academic year. It focuses on the quality of the learning offer in terms of the outcome for individual learners. Programmes are at the core of the framework with each programme attracting a funding value and having a defined purpose and outcome against which it will be monitored. For 2017/18 only eligible programmes will be funded.

CHAPTER EIGHT

Housing

Local authority responsibility for housing is a function of district, metropolitan and unitary councils and London boroughs. Social housing is provided by different types of organisations:

- councils, which manage their own housing stock and deal directly with tenants
- arm's-length management organisations (ALMOs), which are separate bodies set up by councils to manage their housing stock and deal with tenants. Councils still own the housing managed by ALMOs but the ALMO takes over its running. There are no ALMOs in Wales
- registered providers (also known as housing associations), which are completely separate from councils and are not-for-profit organisations that have their own housing stock. These providers are regulated by government.

HOUSING REVENUE ACCOUNT

Councils with more than 50 social houses are required to maintain a separate account that contains all the income and expenditure relating to their housing stock. This account is called the housing revenue account (HRA) and is essentially an account for a council's activities as a landlord. The account records the income and expenditure necessary to manage and maintain the housing stock, including major repairs, and associated debt financing charges.

The HRA is a separate or ringfenced account, meaning that funds must be kept separate from other local authority income and expenditure, to make sure that council housing rents are not used to subsidise general council expenditure and that the general council tax payer does not subsidise council housing. Any surplus in year must go to a separate reserve (or working balance) to only be used for the HRA. Councils must not budget for a deficit on their HRA after the working balance is taken into account.

Other local authority housing activity that is not part of its role as a landlord, and which therefore does not fall within the HRA, is paid for by the general fund of the council.

SELF-FINANCING IMPLEMENTATION

Before April 2012, there was a complicated national housing subsidy system. Government estimated the costs and income for each authority based on assumptions about rent levels and the costs of running and maintaining properties. If the assumed costs were greater than the assumed income, then the council would receive a subsidy. If the assumed income was greater than the costs then the council paid negative subsidy over to the government. In the final years of the subsidy system the amount of negative subsidy paid to the government far exceeded the subsidy that the government was paying out. So council rent payers were net contributors to the exchequer.

Since April 2012, when the concept of a self-financing HRA was introduced, each council became reliant on its own rent income to provide and manage council housing. The government calculated the amount of notional (ie theoretical) debt that each council's HRA could support utilising a 30-year future calculation of its rental income less the notional expenditure for that period. The debt that this sum could support was compared with the government's view of each council's housing debt and HRA debts were adjusted to this level, with some authorities taking on extra debt and making an equivalent payment to HM Treasury, and others having their debt reduced by the Treasury. The final settlement saw £5.3bn repaid by the government, while £13.4bn was paid to government by local authorities. However, since this settlement the government has made a number of significant changes around rent policy, welfare benefits and right to buy that have materially affected the total rental income.

INCOME AND EXPENDITURE

If considered purely as a business, council housing in England is worth about £9.5bn annually, with tenants funding the majority of this via their weekly rent, which for 2015/16 was £87.81 on average.

The rent restructuring programme began in 2002/03 and was meant to last ten years. The aim was to bring council rents more in line with those of housing associations. This was done by setting targets known as formula rents. Formula rents are based on local earnings levels and property values and are increased annually at half a percent over the rate of inflation (as measured by the Retail Price Index) because rents needed to increase by more than inflation in order to catch up with housing association rents. The scheme was made more complicated by rules on the amount any individual tenant's actual rent could increase and by rent caps based on the number of bedrooms in a property. As part of the 2013 spending round the government announced that from 2015/16 social rents would rise by Consumer Price Index plus 1% each year for ten years. Guidance released in May 2014 confirmed that the government would end the rent convergence policy in April 2015.

In an unexpected development, the summer Budget in July 2015 then announced a rent decrease of 1% a year for the next four years to be implemented by housing associations and local authorities and the immediate cessation of rent restructuring. It is estimated that these changes reduce the income receivable over the remaining years of self-financing by around 15%. The recent Housing White Paper reconfirmed the 1% decrease per annum until 2020, although it commented that consideration is being given to rent policy from that date forward. Many commentators have expressed concerns for the implications of these reductions on the business plans and future building projects of the sector, although the full long-term implications are not yet clear.

Local housing authorities may also make separate service charges to tenants for those services, such as a concierge service or community aerials, which are not available to every tenant. In some accommodation there are communal heating systems, the costs of which councils recover from individual tenants by separate charges. Separate services may also be levied for services such as individual garages or parking spaces.

HRA BUSINESS PLANS

All the changes explained above have demonstrated that business planning for the HRA is critical. Housing authorities must be able to show that they can afford to maintain their housing stock and provide services to tenants over the long term. The HRA business plan looks at long-term investment needs, covering 30 years. In preparing the business plan, councils need to assess the right balance between expenditure on long-term planned maintenance and the more reactive repairs when things go wrong. Self-financing gave councils more freedom to balance this relationship to achieve the best value for money, but the changes to income and the restrictions on how much councils can borrow for housing limit a council's ability to invest in social housing in its area. For these reasons, business plans should be regularly reviewed.

HOUSING ALLOCATIONS

Local housing authorities often work with local housing association partners, operating joint waiting lists and allocation policies. This is a function financed by the general fund of the council. The DCLG's Allocation of Accommodation: Guidance for Local Housing Authorities in England (2012) sets out the factors that councils should take into account in framing their allocation scheme to offer a choice of accommodation to applicants. It included guidance on the freedoms introduced by the Localism Act 2011, which gave local housing authorities more flexibility in deciding who is eligible to go on to their waiting lists. Certain categories of applicants (such as returning members of the armed forces) are eligible for inclusion.

Councils are able to offer flexible two-year tenancies in addition to traditional secure tenancies. The government is yet to announce any timescale for the implementation of the fixed term tenancies policy that was part of the Housing and Planning Act 2016.

HOMELESSNESS

Housing authorities are required to provide advice and assistance to homeless people or those in danger of becoming homeless. The cost of this activity falls on the general fund of the council. They also have to provide accommodation to people who are unintentionally homeless and in priority need. This has generally been through providing initially temporary, often expensive and private, accommodation before moving into council or housing association housing. Under the Localism Act 2011, councils can now also offer a year's good quality private sector tenancy to fulfil this requirement.

Housing authorities must maintain a homelessness strategy. A revenue grant allocation is made by the DCLG to help housing authorities meet their homelessness duties.

The Homeless Reduction Act 2017 aims to refocus English local authorities on efforts to prevent homelessness, including an extension of the period during which an authority should treat someone as threatened with homelessness from 28 to 56 days.

WELFARE REFORM AND HOUSING BENEFIT

Housing benefit cost over £21bn in 2015/16 and has been identified by central government to be a prime area for spending reductions. The government has begun to introduce a new system of universal credit and this is expected to replace most housing benefit (and a number of other benefits).

As part of welfare reform, the government has also cut housing benefit support for claimants in temporary accommodation and placed limits on the amounts of housing benefit that will be paid. Local housing allowance rates place limits on the level of rents that will be supported. Previously this limit was based on average rents in the area; now it is based on a lower amount. There is also a limit being placed on the size of house that is used to calculate housing benefit, the 'spare room subsidy' (more often referred to as the 'bedroom tax'), where for example a family occupying a three-bedroom house who would only be entitled to a two-bedroom house under the new rules will still receive housing benefit, but based upon local rental costs for two bedrooms.

The Welfare Reform and Work Act 2016 contains a number of changes that will impact on housing. These include:

- removing the family premium from housing benefit
- limiting the backdating of working age housing benefit claims to four weeks
- removing entitlement to housing support in housing benefit and universal credit for those aged 18–21, replacing it with a youth obligation that will give more intensive support for unemployed youths before mandating them to go on a work placement.
- local housing allowance rates to be frozen for four years
- local housing allowance rates to apply to social housing from 2018
- £800m additional grant to local authorities over the next four years for discretionary housing payments
- changes to the temporary absence from home rules for working age and pensioner claimants leaving the UK for longer than one month.

RIGHT TO BUY

Since the 1980s over 2m council properties have been sold under the right to buy scheme, nearly 50% of the (then) total. The recession and tighter rules on discounts caused the volume of right to buy sales to fall away considerably in later years and in 2011/12 just 3,080 sales were completed, generating capital receipts after discount of £238m.

In 2012, however, the government raised the discounts in England to increase or 'reinvigorate' right to buy sales with receipts from sales (after allowable costs, repayment of housing debt and currently forecast receipts for councils and central government) used to replace the additional homes sold as a result of the higher discount levels.

The DCLG has reported that over 50,000 homes have been sold since its reinvigoration of the right to buy discounts. Councils may retain some right to buy receipts subject to specific rules set out by the government (see Reinvigorating Right to Buy and One-for-One Replacement Consultation: Summary of Responses and Government Response, DCLG, 2012).

Housing association tenants have been promised that they will be allowed to buy their own homes following a voluntary agreement between the National Housing Federation and the government. The Housing and Planning Act 2016 suggests that this should be funded by forcing local authorities to sell off their higher value council houses as and when they become vacant. Details of how this would operate still have not been released. However, announcing a pilot, the housing minister suggested that the scheme would not be operational until 2018.

LEASEHOLDERS

Because of right to buy, many former council estates are now a mix of tenanted property and owner occupation (many of whom are leaseholders). Local housing authorities try to ensure that leaseholders pay their fair share of estate costs (for services such as maintaining lifts) in order to avoid unnecessary expense to the housing revenue account. However, the rules on recovery are complex, especially where major works are concerned, such as re-roofing a block of flats.

For five years after a right to buy sale is completed, only works identified in the sale documentation can be recharged to leaseholders. Leaseholders have statutory rights to loans if works exceed a certain value, and councils can operate more generous local loan schemes.

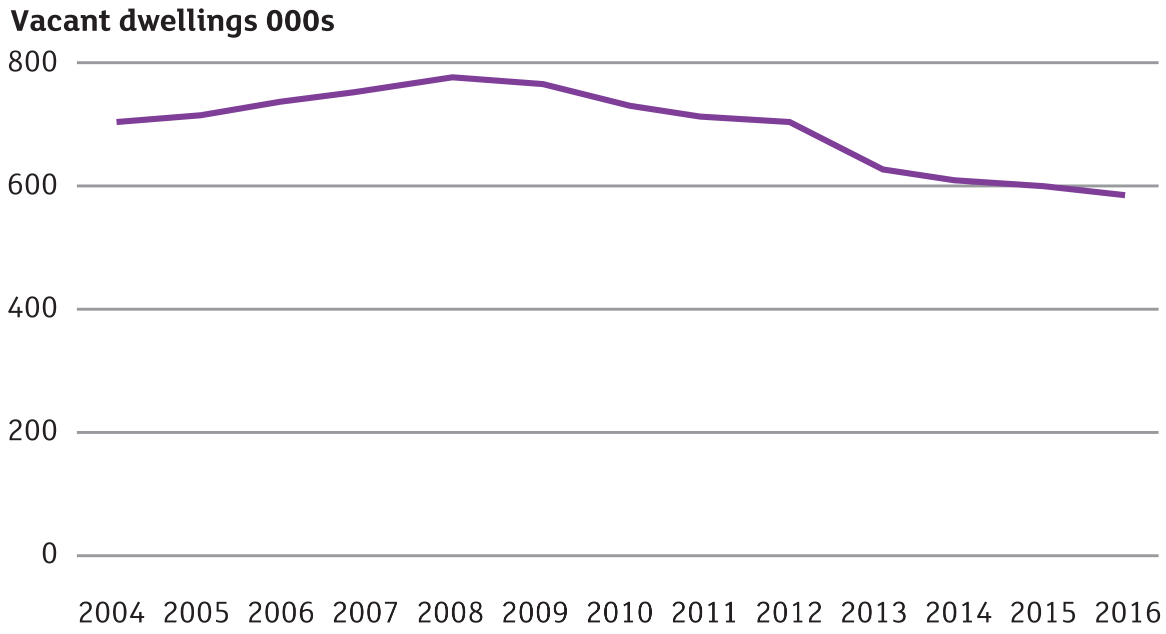
GYPSIES AND TRAVELLERS

Local housing authorities and county councils provide and operate sites for Gypsies and Travellers.

EMPTY HOMES

In October 2015 approximately 600,000 homes in England were empty, and around 200,000 of those had been empty for over six months. Local councils have a key role in identifying empty homes and working with owners to bring them back into use. The New Homes Bonus is a grant that can be paid by central government to local councils for increasing the number of homes and bringing empty homes back into use. The graph below shows that there has been a gradual reduction in empty homes since 2008.

Number of vacant and long-term vacant dwellings, England, 2004–2016



Source: DCLG Table 615 All vacant dwellings by local authority district, England, from 2004

PRIVATE SECTOR LICENSING AND HOUSES IN MULTIPLE OCCUPATION

Councils must keep the housing conditions within their area under review. Under the Housing Act 2004 a housing health and safety rating system is used to determine whether the authority needs to intervene. Local councils may decide to introduce a licensing system for specific categories of rented property. A common problem found in many local areas is the overcrowding and increased fire risks associated with housing in multiple accommodation.

SHELTERED HOUSING

Local housing authorities provide sheltered supported or extra care properties. Some of this accommodation is hard to let, and councils find it difficult to identify funding for modernisation. Yet expenditure on sheltered housing can mean larger savings on care homes and other more costly support.

The need for sheltered housing is increasing as the country's ageing population grows, while the profile of users is altering with regard to vulnerability (eg substance abuse).

A proposal to apply the local housing allowance in sheltered housing has been subject to a consultation with many expressing concerns that the future of this type of accommodation would be threatened by such a move at the very time that the nation's population is getting older.

DECENT HOMES STANDARD

The decent homes standard set out, essentially, that all homes should be warm, weatherproof and have reasonably modern facilities. It applies to social rented housing (predominantly council or housing association housing).

The broad principle is that a home must have reasonably modern facilities. The specified requirements are as follows.

- The home must meet the statutory minimum standard for housing (under the housing health and safety rating system). It will therefore not have any safety hazards (such as a sub-standard gas heating boiler).
- It must be in a reasonable state of repair. No key building component should be too old and need replacing. (Key building components are items such as walls, roof, windows and the heating system.) Not more than one other building component should need replacing.
- It must have reasonably modern facilities and services. In particular the kitchen should be less than 20 years old and the

bathroom less than 30 years old. Not more than two of the main facilities may be too old.

- It must provide a reasonable degree of thermal comfort. This means an efficient heating system, and good insulation.

Many councils achieved the decent homes standard for their housing by 2012. However, the self-financing settlement did not contain sufficient resources to enable councils to achieve the standard if they had not already done so. The government allocated a further £160m investment in the decent homes programme, targeted at those councils with the biggest backlogs of repairs, in the 2013 spending review. The term ‘decent homes plus’ refers to environmental and estate works that go beyond the narrow purpose of decent homes.

As of 1 April 2016 there were 79,900 ‘non-decent’ local authority owned dwellings across England, a 24% reduction on the previous year.

THE HOUSING WHITE PAPER – FIXING THE BROKEN HOUSING MARKET

Issued early in 2017, this White Paper consulted on a move away from an emphasis on home ownership and detailed the government’s view on how the current housing crisis can be addressed via a number of key initiatives. These included proposals to simplify the planning system, to ensure permissions granted are acted upon, to bring small and medium sized builders back into the market, working with local authorities to help them build and to address the need for starter homes. The government’s response to this consultation is awaited.

CHAPTER NINE
Social care

Social care is a function carried out by county, metropolitan and unitary councils and London boroughs. Social care has long been, after education, the second largest area of expenditure within councils and the largest under effective local control. With the increase in academies, changes to education funding and the rising demand for social care, it is likely that social care will become the largest service provided through councils. The budgeted net current expenditure in relation to adult social care for England in 2016/17 was £14.4bn (Wales £1.0bn). For children's social care, the total was £7.8bn (Wales £0.7bn) making the total budgeted net expenditure for social care £22.2bn (Wales £1.7bn).

ADULT SOCIAL CARE

Adult social care includes services for elderly people and a wide range of services for those in the 18- to 64-years age group. Budgeted expenditure for adult social care in England for 2016/17 was £14.4bn (Wales £1.0bn).

Services for older people consume 45% of the money allocated for adult social care. Services for people with learning disabilities are the second largest element of the adult social care budget, accounting for 35% of the money allocated. Accounting arrangements have, however, recently been amended to focus more on the nature of support required (whether difficulties are physical/sensory/memory and cognition/learning disability/mental health) rather than the age group supported. This will allow a more sophisticated analysis of future spending patterns.

Other adult care services include those for people with physical disabilities, sensory impairment and mental health needs, and asylum seekers.

Demand-led Pressures

Adult social care is a demand-led service. This means that if a person is assessed as needing care and that care is within the eligibility range set by the national rules introduced by the Care Act 2014, then the person must receive that care. Historically, this has made social care one of the most difficult budgets to manage. The key actions are:

- to fund and encourage preventative support in the community to reduce the chances of people requiring individualised help
- where such support is needed, to intervene early enough in a client's care to prevent long-term admission to residential care, which is an expensive commitment
- to use short-term intensive reablement packages to return people to independence following hospitalisation, and so avoid long-term support where possible.

The large growth in the population aged over 65 and especially over 80 has increasingly focused the attention of both local and national government on the demands on adult social care, particularly long-term care. That, together with reductions in government grants to local authorities, has led councils to implement a wide range of savings measures.

Pressure on Social Care Budgets

In its autumn 2016 Budget submission, the Local Government Association assessed the demand on adult social care budgets in England to rise from £14,380m in 2016/17 to reach £17,833m in 2019/20 – additional pressure of about £3.5bn.

Adult social care – forward cost projection to 2019/20

2016/17 baseline spend	2017/18	2018/19	2019/20
£m	£m	£m	£m
14,380	15,444	16,629	17,833

Source: Local Government Association

The government responded to this assessment by permitting council tax increases for social care which are additional to any general increase for which referendum requirements still apply. So, from 2016/17 social service authorities could increase the council tax by an extra 2% per year with no referendum requirement, provided the additional income raised is dedicated to social care. This will yield £400m per year if all authorities choose to implement it, ie an extra 1.8% on current budgets for social care. There was been a broad consensus within local government that this is helpful, but not in itself sufficient to enable rising social care demand to be met. There was also criticism of the distributional aspects.

The government responded to some of these comments with further measures:

- The council tax precept for social care, while still required to average no more than 2% per year over the three period to 2019/20, can be frontloaded by being set at 3% in 2017/18 and 2018/19.
- Additional direct funding is being provided of £1.2bn in 2017/18, rising to £2bn by 2019/20 (after which the Improved Better Care Fund will, as explained below, provide the mechanism for a similar level of funding). This additional funding is skewed towards those authorities with the lowest tax bases – who are both able to raise proportionately less money through the social care precept but are likely to face the sharpest increases in social care demand.
- A Green Paper has been announced, to be published in late 2017, designed to tackle the long-term underlying funding issues in the sector.

Paying for Care

The charging systems in England and Wales follow similar principles.

Residential care is means tested and based on a national system in each area. Capital assets such as property are taken into account after 12 weeks when the residential stay is permanent. If a service user has sufficient resources, they will pay for the full cost of the service until their resources fall below a certain limit. Charging for non-residential services is discretionary and the policy is determined locally within a nationally set framework. Generally, for these services property is not taken into account. In Wales the cost of non-residential care is capped at £50 per week. In England the maximum cost is set locally.

The Care Act 2014 incorporated plans to introduce, from April 2016, a £72,000 cap on care costs in England. This would have limited the amount anybody would pay for social care over their lifetime to £72,000, although for anyone in residential care, this would not include living costs such as food, energy bills and accommodation. In reality, the care cap was only likely to directly benefit those with high care needs over a long period. Importantly though, by reducing the impact on those individuals, it would have mitigated the concern of everyone that they too might fall into that group later in life. In July 2015, however, the government announced a delay in implementation from 2016 to 2020, in the light of perceived difficulties with practical implementation and cost.

During the 2017 general election campaign, the prime minister indicated that a cap would be introduced, but that the amount at which it would be set was to be reviewed. Further potential changes were announced, to be incorporated into a planned Green Paper on the financial system for social care, including taking property assets into account for home care as well as residential care through a system of deferred charges, and raising the limit below which charges do not apply from £23,250 to £100,000.

The Welsh Government is currently considering its approach to the cost of long-term care and whether a cap on residential care costs should be introduced in Wales.

CHILDREN'S SOCIAL CARE

Budgeted expenditure for children's social care for 2016/17 was £7.8bn for England and £0.7bn for Wales.

Looked after children account for the largest proportion (45%) of this expenditure, with commissioning and social workers (20%) being the second largest element. Other services include youth justice work, family support and support for asylum seekers.

Children's social care is like adult social care also demand led. If a child is placed into a local authority's care, then that child must be supported, with residential placements being the most expensive. As with adult social care, the policy focus is to intervene early in order to both prevent expensive admission into care and provide better outcomes for children in their own homes.

The government estimates that £8bn is spent on 120,000 families with multiple problems that can furthermore continue across generations. A consequence of this complexity is that support has often been unco-ordinated, reactive and costly to a range of public services such as police, local authorities, health, housing and probation. The government therefore invested in a national Troubled Families Programme, offering incentives to all upper-tier authorities to turn around the lives of this specific group of families.

The Local Government Association's autumn 2016 Budget submission, using a broad definition of children's services, assessed the demand faced by local government in England to be increasing from £11,142m in 2016/17 to £12,092m in 2019/20 – additional pressure of roughly £0.9bn.

Children's social care and education services – forward cost projection to 2019/20

2016/17 baseline spend	2017/18	2018/19	2019/20
£m	£m	£m	£m
11,142	11,419	11,762	12,092

Source: Local Government Association (includes services funded through the Education Services Grant)

HEALTH AND SOCIAL CARE INTEGRATION

While community budgets have been the primary driver for integration in children's services, the government has more recently sought to boost the pace of integration in adults' services through new initiatives.

In 2015/16 the Better Care Fund required at least £3.8bn to be used to advance integrated transformation of health and social care. The government encouraged additional contributions to be made through local decisions, and the fund as finalised totaled £5.3bn. The spending review in 2015 announced that the Better Care Fund would remain in place and set out plans for a £1.6bn increase in its size by 2020/21. This forms the basis for pooled budgets for health and social care to work more closely together in local areas, based on plans agreed between the NHS and local authorities. It has been described as "the biggest ever financial incentive for councils and local NHS organisations to jointly plan and deliver services, so that integrated care becomes the norm by 2018".

The Better Care Fund offers a real opportunity to address immediate pressures on services and lay foundations for a more integrated system of health and care delivered at scale and pace. But it will create risks as well as opportunities. The £3.8bn was not an addition of new money into the social care system, leaving the organisations commissioning services to make important decisions about how the funding transfer can make a positive difference to social care services and outcomes for service users.

Clinical commissioning groups and councils had to jointly agree plans for how the money will be spent. These plans must meet certain criteria and must be signed off by health and wellbeing boards and NHS England.

Consistent with that approach, in 2015 the government agreed a £6bn plan to devolve all health and social care in the Manchester conurbation to local control. Further agreements have followed, and though not all have incorporated joint working with health, this could well provide the major part of the future template for integration. The government requires all local health and social care economies to submit, by 2017, plans for how they will pursue full integration by 2020.

This expectation remains in place, but no further detail has followed, and it now appears that this agenda will be taken forward mainly through the introduction of sustainability and transformation plans (STPs), which are integrated place-based plans for the future of health and care services in each of 44 areas into which England has been split. They are five-year plans covering all aspects of NHS spending in England from 2016/17 to 2020/21. Social care is not necessarily covered directly, but is seen as a critical consultee and part of the overall picture. All 44 plans – as submitted in draft in October 2016 – are now publicly available for consultation and ongoing development.

There is no equivalent central requirement for STPs in Wales, where there are seven local health boards (with no purchaser-provider split) and 22 local authorities. The Welsh Government asked local authorities to merge voluntarily but with little result. Local examples of integration, such as the Gwent Frailty Programme, present a potential way forward, with the health board and five local authorities pooling their budgets, and such initiatives could lead to developments akin to STPs.

CHAPTER TEN
Police

Policing in England and Wales was radically reformed in 2012 with the introduction of police and crime commissioners, who are responsible for commissioning police services in their areas as well as services related to crime and anti-social behaviour. This means that they are responsible for setting the overall budget for police services and setting the priorities and objectives for policing for their local areas.

The police and crime commissioner is a directly elected individual. The chief constable remains responsible for delivering policing in their area in accordance with the budget, priorities and objectives set by the police and crime commissioner. The police and crime commissioner holds the chief constable to account for delivery. Both the police and crime commissioner and the chief constable have been established as separate organisations, which has implications for police finance.

There are special arrangements in some areas. In London the mayor has responsibility for policing, apart from in the City of London, which has a police committee for its police force. The creation of a metro-mayor in Greater Manchester from May 2017 meant that a separate PCC in Greater Manchester no longer exists as the mayor has taken over this function within the combined authority for Greater Manchester. The chief constable remains a separate legal entity, accountable to the mayor as PCC.

The Policing and Crime Act 2017 may also lead to some police and crime commissioners taking on the governance of local fire and rescue services and potentially merging their local police force and fire and rescue services into a single employer with a single chief officer reporting to the police and crime commissioner.

EXPENDITURE AND BUDGETS

Total funding for policing for 2016/17 was £10.4bn in England (excluding national Home Office reallocations to support national priorities) and

£0.61bn in Wales. From April 2013, policing has been paid for by a mixture of council tax and Police Grant received from the Home Office. Police are not part of the localisation of non-domestic rates regime (see Chapter 1) but are affected by the localisation of support for council tax. The police and crime commissioner is responsible for setting the council tax for policing for their area as well as the overall police budget.

FINANCIAL MANAGEMENT

The Financial Management Code of Practice for the Police Service for England and Wales, updated in 2013 by the Home Office, sets out key principles that police and crime commissioners and chief constables must follow as well as a protocol for how the two organisations work together. The police and crime commissioner must decide how much financial freedom to give to the chief constable, and this will vary from area to area. There are, however, a few important principles that must be followed.

- Responsibility for setting the policing precept must stay with the police and crime commissioner.
- The police and crime commissioner retains responsibility for the police fund (this is the equivalent of the general fund in councils and manages all income and expenditure and reserves that are the ultimate liability of the council tax payer).
- The chief constable can only borrow money with the consent of the police and crime commissioner and only for the short term and cannot enter into credit arrangements which are transactions giving rise to a liability other than that to repay money, so that all borrowing for capital investment is undertaken by the police and crime commissioner.
- Initially, all liabilities for employees remained with the police and crime commissioner, but in April 2014 staff and some assets were transferred to chief constables under what is known as ‘stage two’ transfers. The extent of stage two transfers varied from area to area.

It is important that individual police and crime commissioners pay careful attention to the financial arrangements they put into place as there is no single solution. They will have to implement arrangements that reflect local circumstances.

STATEMENT OF ACCOUNTS

Both the police and crime commissioner and the chief constable will need to produce their own statement of accounts. The police and crime commissioner then has to bring these together into something called the group accounts, which show the total costs of policing for the whole area. The individual accounts of the police and crime commissioner and the chief constable will each have a large single item relating to money passed from the police and crime commissioner to the chief constable; these will cancel each other out in the group accounts.

Key definitions

Accounting Standards	Rules set by the International Accounting Standards Boards that set out how transactions are to be shown in an organisation's accounts.
Accrual	The recording of income and expenditure when it becomes due rather than when cash is paid out/received.
Aggregate Start-up Funding Assessment	The amount of central government money to be allocated to local government to calculate the start-up position for the non-domestic rate localisation system.
Annual Statement of Accounts	An annual statement setting out the income and expenditure of the council along with its assets and liabilities.
Arm's-length Management Organisation	An organisation set up by the council to manage its council housing on its behalf.
Audit Committee	A special committee of the council that reviews the financial management and accounts of the council.
Balance Sheet	A statement showing the assets and liabilities of the council.
Baseline Funding Level	The proportion of the start-up funding assessment to be funded from locally retained business rates.
Billing Authorities	District, unitary, metropolitan and London borough councils who collect council tax and non-domestic rates on behalf of all local councils.
Budget Requirement	The amount a council needs to fund its spending from council tax, non-domestic rates and Revenue Support Grant.
Capital Budget	The money a council spends on investing in new buildings, infrastructure and expensive pieces of equipment.
Capital Financing Charges	The amount a council has to pay to support its borrowing to pay for the purchase of major assets.
Capital Receipt	The money a council receives for selling assets that can only be used to repay debt or for new capital expenditure.
Cash Flow Statement	This statement summarises the cash flows that have been made into and out of the council during the year.

Chief Financial Officer	The most senior finance person in a council responsible for ensuring the proper financial management of the council.
Code of Practice on Local Authority Accounting in the United Kingdom	A code produced by CIPFA/LASAAC that sets out how councils should show transactions in their accounts and the format of the accounts.
Collection Fund	An account used by a billing authority to pay in the council tax and non-domestic rates it collects and to pay the income to itself and its major preceptors.
Community Budget	A budget created by a number of public sector organisations combining their resources.
Comprehensive Income and Expenditure Statement	This statement shows all the income and expenditure of the council.
Council Tax	A tax paid by local domestic households to their council.
Dedicated Schools Grant	A grant that has to be used by councils to fund schools.
Deficit/Surplus on the Collection Fund	The difference between the amount of tax estimated to be collected and the amount actually collected.
Depreciation	The charge to the comprehensive income and expenditure statement for the use of assets.
Earmarked Reserve	Money set aside for future use on a specific area of expenditure.
Estimated Business Rate Aggregate	The total amount of business rates that the government estimates will be collected by councils in total.
External Audit	An external review of the council's accounts and systems.
Funding Formula	A mathematical formula based on population, deprivation and other local indicators to allocate the aggregate start-up funding assessment between individual local councils.
Governance	The framework by which a council can gain assurance that it is setting and achieving its objectives and ensuring value for money in the proper way.

Housing Revenue Account	An account used to record the income and expenditure related to council housing.
Internal Audit	An internal review of the organisation's systems to give assurance that they are appropriate and being complied with.
Levies	Amount collected by special-purpose bodies from councils, including flood defence and in some areas public transport.
Levy (Non-domestic Rates)	A proportion of non-domestic rate growth above inflation that a council has to pay into the central pot.
Local Councils or Local Precepting Bodies	Parish, town and community councils.
Local Government Control Total	The amount of the overall public spending envelope the government decides should be spent by local government.
Local Government Finance Settlement	The annual announcement by the government and the Welsh Government on the amount of resources they will give to local government.
Major Preceptors	County councils, the Greater London Authority and police and fire authorities who collect their share of council tax through a precept on their billing authority.
Movement in Reserves Statement	This statement shows the impact of the financial year on the council's reserves.
Net Revenue Expenditure	The amount a council spends on providing services after capital financing costs and specific government grants are taken into account.
Non-domestic Rates	A tax paid by local businesses to their council.
Precept	The total amount of council tax county councils, the Greater London Authority and police and fire authorities require billing authorities to collect on their behalf.
Principal Local Authorities	County councils, district councils, unitary councils, metropolitan councils, London boroughs, the Greater London Authority and police and fire authorities.
Proportionate Shares	An individual council's estimated share of the estimated business rates aggregate based on the proportion of the total business rate income it has collected over the past two years.

Provision	Money set aside against a specific future liability.
Prudential Code	A code produced by CIPFA that councils are required to follow when deciding upon their programme for capital expenditure.
Pupil Premium	An amount that is paid to schools by the government for each of their pupils that are classified as deprived.
Registered Provider	A not-for-profit organisation that provides social housing.
Revenue Budget	The amount that a council spends on its day-to-day running of services through the financial year.
Revenue Support Grant	General grant paid to councils by the government to support their expenditure.
Right to Buy	The right of council tenants to buy their council houses at a discount.
Ringfencing	A term for the earmarking of money (eg a grant or fund) for one particular purpose, so as to restrict its use to that purpose.
Safety Net	Funding from the central non-domestic rates pot that is used to support councils whose rate income has fallen by more than 7.5% in any one year.
Schools Funding Formula	The formula that is used to distribute funding between individual schools.
Specific Government Grants	Grants given to councils by central government to fund specific services or projects.
Standard Spending Assessment	An individual council's share of the local government spending control total for Wales.
Start-up Funding Assessment	An individual council's share of the aggregate start-up funding assessment as calculated by the funding formula.
Top-up and Tariff	The amount of local non-domestic rate income that an individual local authority has to pay in to/receives from the central pot.
Total Service Expenditure	The amount a council spends on providing services before capital financing costs and specific government grants are taken into account.

Trading Account	An account used to record the income and expenditure of a part of the council that is engaged in trading activities.
Treasury Management	The management of the cash balances and borrowing needs arising from the council's cash flows.
Treasury Management Code	A code produced by CIPFA that councils are required to follow in managing their treasury management activity.
Treasury Management Strategy	An annual document approved by full council that sets out how a council will manage its cash and borrowings.
Valuations Office Agency	The government agency responsible for valuing domestic and non-domestic properties for local tax purposes.

Further reading

Please visit www.cipfa.org/publications for more information.

Balance Sheet Management in the Public Services: A Framework for Good Practice (2017 Edition), CIPFA, 2017

Balancing Local Authority Budgets, CIPFA, 2016

CIPFA Statement on the Role of the Chief Finance Officer of the Police and Crime Commissioner and the Chief Finance Officer of the Chief Constable, CIPFA, 2012

Code of Practice on Local Authority Accounting in the United Kingdom, CIPFA, annual

Delivering Good Governance in Local Government: Framework (2016 Edition), CIPFA/Solace, 2016

Delivering Good Governance in Local Government: Guidance Note for Policing Bodies in England and Wales (2016 Edition), CIPFA, 2016

The Guide to Local Government Finance, CIPFA, annual

A Guide to Local Government Taxation and the Collection Fund, CIPFA, 2014

Housing Finance under Self-financing, CIPFA, 2013

Investing in Council Housing, CIPFA/CIH, 2016

Practitioners' Guide to Capital Finance in Local Government (2012 Edition), CIPFA, 2012

The Prudential Code for Capital Finance in Local Authorities, CIPFA, 2017

The Prudential Code for Capital Finance in Local Authorities: Guidance Notes for Practitioners (2013 Edition), CIPFA, 2013

The Public Sector Internal Audit Standards, the Relevant Internal Audit Standard Setters, 2017

A Risk-based Approach to the Audit of Procurement (2015 Edition), CIPFA, 2015

The Role of the Chief Financial Officer in Local Government, CIPFA, 2015

The Role of the Head of Internal Audit in Public Service Organisations, CIPFA, 2015