Financial Management Code: Financial Resilience Assessment

Purpose

CIPFA's Financial Management (FM) Code recommends that local authorities undertake a financial resilience assessment (FRA) each year. The FRA builds on the one-year assessments required under section 25 of the Local Government Act 2003 of the robustness of the estimates used in the budget calculations and the adequacy of the proposed levels of financial reserves.

Context

CIPFA states that "effective governance and financial management is focused on ensuring that the authority is able to operate sustainably in the long term. This means that the authority needs to look beyond the limited time horizons of its funding arrangements and to consider the longer-term financing of its operations and activities."

The financial resilience assessment considers long-term financial stability. It does so by considering warning signs such as the symptoms of financial stress and reviewing how effectively the authority manages its finances. This includes explicit consideration of capital resources, reserves, savings plans and the use of performance information. The FM Code requires that the authority demonstrates how the risks identified through a financial resilience assessment have informed the development of its longer-term financial strategy.

Approach

Pre-requisites for the financial resilience assessment are the council's strategic plan (Borough Plan) and financial strategy (MTFS). The FM code recommends the technique of scenario planning to inform their development. For capital CIPFA's Prudential Code provides a framework for the self-regulation of the authority's capital financing arrangements. The financial resilience assessment reviews how effectively the council delivers the aims of the Prudential Code. It also considers how the Council develops a suitable Capital Strategy and how it sets and reviews the various indicators required under the Prudential Code.

Medium Term Planning

The Medium Term Financial Strategy translates the authority's financial strategy into a plan for the near future. Before a financial resilience assessment can be undertaken, the Council needs develop a robust medium-term financial plan that coordinates and integrates financial and service planning, capital financial management, risk management and asset management plans. This needs to be linked to the long-term financial planning process that the FM Code advocates together with adoption of a robust cycle of the financial year that will become a feedback loop to inform the financial planning process.

Long Term Planning

A full and thorough financial resilience assessment can only be undertaken once the Council's service and financial planning framework has moved to a more long-term and better joined up position with a clearly linked and articulated Medium Term Finance Strategy, a Long Term Financial Strategy, Borough Plan, Service Plans and Capital Strategy. These plans need to be seen as dynamic documents which are subjected to sensitivity analysis using techniques such as scenario planning and risk management to ensure that the Council's finances will be sustainable in the long-term.

Reviewing of Current Position

The FRA will consider CIPFA's symptoms of financial stress. These are:

Symptoms of financial stress

Running down reserves	Using the authority's financial reserves to finance a deficit or to avoid difficult decisions around spending cuts. This provides temporary relief, but is not sustainable in the long term.
Failure to address financial pressures	Refusing to make difficult decisions about how to reconcile funding and service pressures, or not recognising that such decisions need to be made. This is equally not a solution to those challenges, but instead simply increases the financial gap and the extent of change that will be required in future years.
Shortened planning horizons	Long-term planning is more difficult in times of uncertainty, but it is still important, perhaps even more so than in more stable circumstances. A failure to plan is indicative of a lack of strategic thinking and an unwillingness to make difficult decisions.
Lack of investment in infrastructure resources	When resources are scarce, it is tempting to defer the maintenance and enhancement of assets (such as buildings) to future periods, which can result in the failure of key physical resources and repairs backlogs that are ultimately more costly than timely maintenance and planned investment in enhancements.
Gaps in savings plans	Knowing that savings are required is helpful, but knowing how these savings are going to be achieved is critical. Simply indicating that 'unidentified savings' will be made is not an acceptable strategy for financial resilience.
Unplanned overspends	No budget is going to be absolutely spot-on. However, overspending against the budget is simply rolling over this year's problems into next year. It is a clear sign that the authority is failing to turn its financial policy decisions into action on the ground.

Ensuring processes deliver financial resilience

This work will cover many of the core financial management process: the MTFS, budget setting process, Capital Strategy, Asset Management Plan, performance management, benchmarking and peer reviews of performance, agreement and management of savings and the effective management of reserves. The main headings are:

Factors for assessing financial resilience

Routine	Getting routine financial management right
Capital	Planning and managing capital resources well
Performance	Using performance information effectively
Savings	Having clear plans for delivering savings
Reserves	Managing reserves well.

Scope of Formal Assessment

The scope for the formal Financial Resilience Assessment is as follows:

Scope

Current	The authority's current financial position
Future	The authority's own assessment of its future financial prospects
Adopted FRF	The extent to which the authority has embraced the financial resilience factors discussed above
Risks	The key financial risks facing the authority, for example by drawing on potential future scenarios including 'best' and 'worst' case scenarios – for the environment in authority operates and for the services that it provides
Independent measures of risk	The use of independent, objective measures to assess the risks to the authority's financial resilience and sustainability.
Associated risks	The authority's understanding of the risks associated with all resources used for service delivery, including its workforce, its physical assets, its strategic business partners (including 'group' entities such as leisure trusts), its information technology infrastructure, etc
Robustness	The robustness of the plans that the authority has put in place to address these risks
Capacity	The capacity and capability of the authority, its leadership team and its officers to manage the authority's finances in a sustainable manner.

Reporting

A financial resilience assessment will result in a clear report to the CMT and Cabinet, setting out an assessment of the Council's financial resilience, together with areas for improvement and how these could be addressed.