

UNIVERSITY OF  
BIRMINGHAM

Birmingham Business School  
Institute of Local Government Studies

Independent review of the  
financial position of  
Birmingham City Council  
Report

August 2012

Independent Review of the Financial Position of Birmingham City  
Council: Report

**The Institute of Local Government Studies (INLOGOV),  
University of Birmingham**

**CONTENTS**

|  |    |
|--|----|
| Introduction .....   | 3  |
| The National Context .....                                     | 3  |
| Birmingham City Council's Financial Position .....             | 6  |
| Future Risks.....  | 8  |
| Equal Pay.....   | 8  |
| Reserves.....  | 8  |
| Closing the Funding Gap .....                                  | 9  |
| Borrowing.....   | 11 |
| Income from Council Tax .....                                  | 12 |
| Council Tax Benefit.....                                       | 12 |
| Business Rates Retention.....                                  | 13 |
| Accounting Issues.....   | 13 |
| The Role of Members in Financial Management.....               | 15 |
| Recommendations .....  | 15 |
| Detailed recommendations .....                                 | 16 |
| Appendix I: References.....                                    | 18 |
| Appendix II: Metropolitan Districts' Non-School Reserves ..... | 20 |
| Appendix IV: Interviewees.....                                 | 22 |
| Appendix V: Developing a New Model for Public Services .....   | 23 |
| Building Stronger Relationships with Residents .....           | 23 |
| Co-production .....  | 24 |
| Behaviour change .....   | 24 |

**FIGURES**

|   |    |
|---|----|
| Figure 1: Overall Public Expenditure and Tax Revenues.....          | 3  |
| Figure 2: Projected Local Government Income Versus Expenditure..... | 4  |
| Figure 3: The Barnet Graph of Doom.....                             | 5  |
| Figure 4: Comparative Council Tax Levels .....                      | 12 |

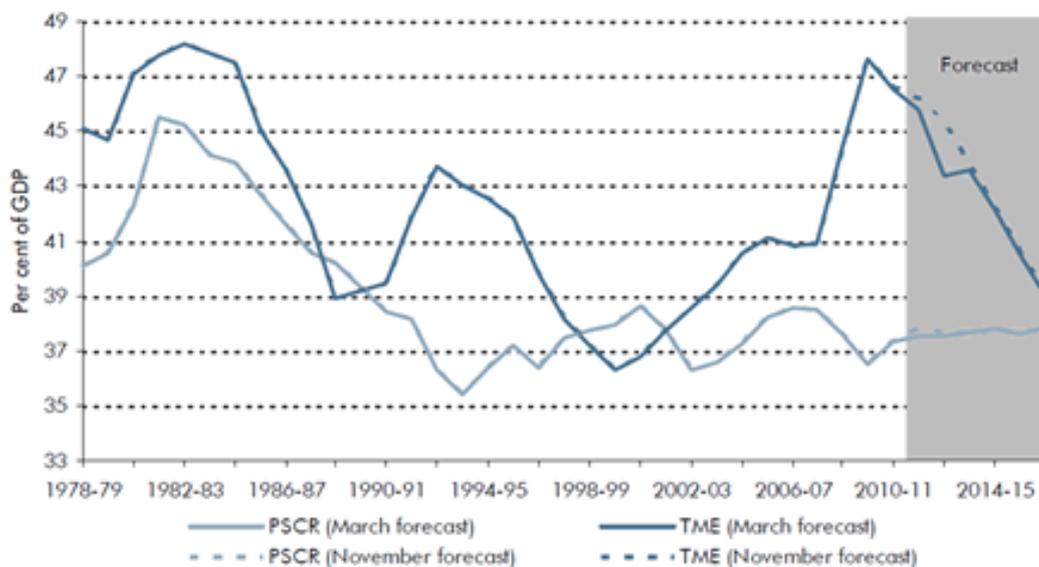
## Introduction

This report summarises the findings of a rapid review of the financial position of Birmingham City Council, undertaken in July and August 2012<sup>1</sup>.

## The National Context

The background national picture of the prospect for government spending is indicated in Figure 1 below, which shows how the Government plans to bring Total Managed Expenditure down towards the level of expected tax receipts. Achieving this reduction in spending implies major and sustained restrictions in public expenditure. From the March 2012 Budget we see that departmental expenditure limits for the Spending Review 2010 period are set to decrease by an annual average rate of 2.3 per cent and to decrease at an annual average rate of 3.8 per cent for 2015/16 and 2016/17 (HM Treasury, 2012, Annex A, p. 86).

**Figure 1: Overall Public Expenditure and Tax Revenues.**



Source: ONS, OBR

Source: <http://budgetresponsibility.independent.gov.uk/total-public-sector-spending-and-receipts-2012-03/>

These are average rates for all government spending, but Birmingham City Council suffered cash reductions of Formula Grant of 10.2% in 2011/12 and 7.2% in 2012/13 (BCC, 2012d p, 84), and the City's planning assumptions of cash reductions of resources from government of 2.2 per cent in 2012/14, 7 per cent in 2014/15, 5.3 per cent in 2015/16 and 7.1 per cent in 2016/17 appear to be well judged (BCC, 2012d, p. 85).

<sup>1</sup> The report was written by a team that included Ron Hodges, Catherine Staite and Peter Watt of the University of Birmingham.

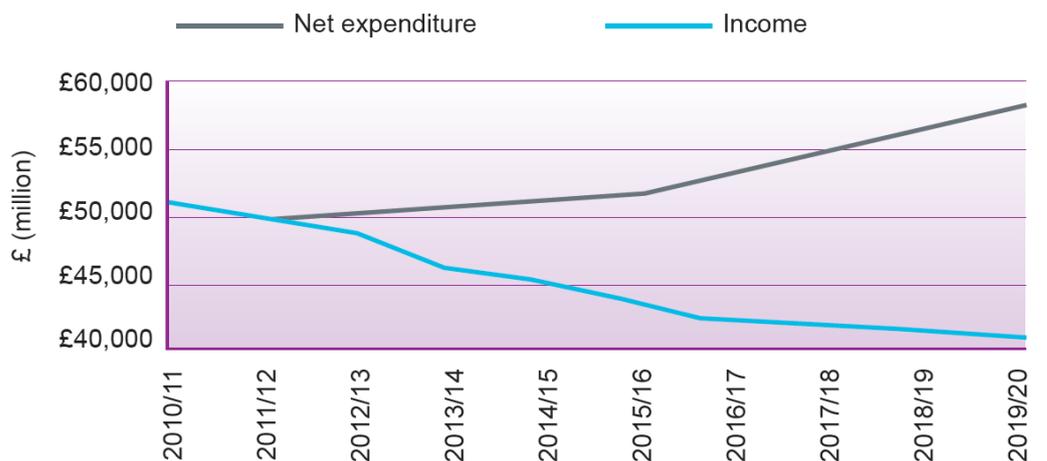
Against this picture of fiscal austerity, national spending needs will be rising rapidly. For example, it is projected that the proportion of the population aged 65 and above will rise from 17 per cent in 2012 to roughly 26 per cent in 2061 (OBR, 2012, p.7).

The Local Government Association (LGA, 2012) has made a projection of future local government spending against future spending needs, and has found that

“A gap opens out in 2012/13 and then continues to widen every year through to 2019/20. The overall funding gap starts at about £1.4 billion in 2013/14 in cash and amounts to over £16.5 billion in 2019/20.” (LGA, 2012, p.8).

Figure 2, based upon assumptions that current trends in local government income and service provision costs will continue through the decade, shows this widening funding gap.

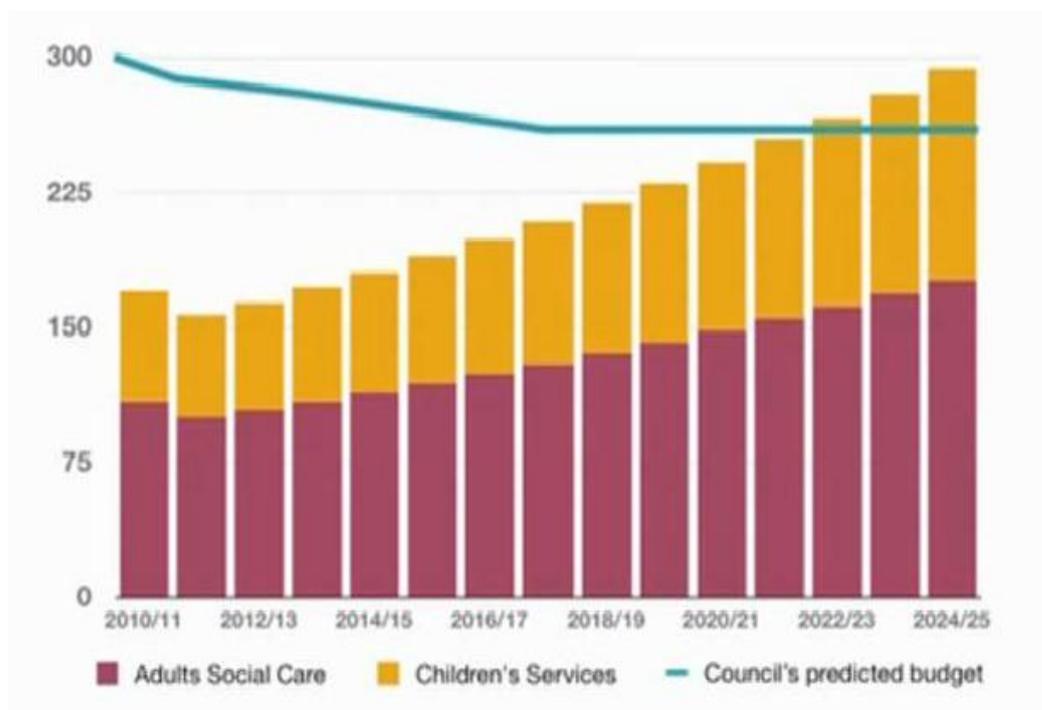
**Figure 2: Projected Local Government Income Versus Expenditure**



Source: LGA (2012, p. 8)

At the level of the individual local authorities, the consequence of the conjunction of growing spending needs and falling spending resources has been illustrated dramatically in the Barnet ‘Graph of Doom’ (Figure 3). The graph shows Barnet Council’s projected available resources being engulfed by rising spending needs for adult social care and children’s services, leaving no room for other areas of council provision.

Figure 3: The Barnet Graph of Doom



Source: <http://inlogov.wordpress.com/2012/05/23/barnet-graph-doom/>

This scenario is likely to apply to many authorities. For those like Birmingham, with a high proportion of their income coming from central government grants, the impact of reductions in their grants on spending power will be more severe than in other areas, despite various forms of transitional relief, in a continuation of the effect highlighted by the Institute for Fiscal Studies

“the cuts in grants between 2009–10 and 2011–12 have generally meant that, across England, high-spending local authorities, which are typically relatively grant dependent, have seen larger cuts to their overall spending power than lower-spending authorities, and have therefore had to make larger spending cuts (both in absolute and in percentage terms)” (IFS, 2012, p.131).

To counter the impact of this severe pressure on resources, Birmingham needs a more developed and better integrated strategic framework for maximising other sources of income and the delivery of savings. In the short term, there will be a need for some services to be decommissioned; otherwise all services will end up being progressively starved of resources. In the longer term the Council will need a strategic approach to managing demand, changing behaviour and maximising co-production - the contribution which residents make to their own wellbeing and that of their families and communities.

The importance of rapid action has been reinforced by risks that have been progressively accumulating in the Council’s finances. In the run up to the election, council tax was frozen and the decision not to proceed with the

adult services *New Offer*, following judicial review, led to a loss of momentum in making savings in a key service area that, by its scale alone, should be an important future contributor to challenging savings targets. After the election, there has been a statement that “we will not be putting up Council Tax this year” (Bore, 2012) but continuing to hold down Council Tax will have a significant impact on the Council’s ability to maximise its income. Figure 4 (below) shows that Birmingham has increased council tax less rapidly than the average metropolitan district. A common political assumption is that there are more benefits to the party in power in delaying potentially unpopular decisions before elections rather than after. Any administration is therefore likely to want to address unpopular but necessary policy issues early in its life, to leave more flexibility in the run-up to the next election. We would expect Birmingham to be no exception, irrespective of political control. The implication is that now is the time for difficult decisions.

Against this background, we have sought to provide a balanced, external review of the financial position of Birmingham City Council. Our review is based largely upon documentary sources ( listed in Appendix I an III), most of which are already in the public domain, supplemented by a small number of interviews. In this report we highlight those issues which we regard as having most significance to the future financial stability of Birmingham City Council – those that represent the greatest risks and opportunities for the Council. We have not conducted an examination of the accounting information systems of the Council and we do not express an opinion on the financial statements of the Council. We have not sought access to the detailed procedures underlying the Council’s budgeting processes and we do not provide forecasts of the extent of achievement towards the Council’s budgetary targets.

## **Birmingham City Council’s Financial Position**

As part of this review of the Council’s financial position, we have considered two time frames. The first was to look back to examine the issues that have faced the Council in recent years and the extent to which the Council, in respect of its strategy and actions, has been successful in responding to the financial pressures that it has faced. The second was to consider the current and likely future financial risk facing the Council and how it might adapt its approach to meet future financial challenges.

Prior to 2010 the Council had enjoyed a relatively limited set of financial pressures and had been able to deal with these within its annual budget, while still providing enough headroom for major projects such as the redevelopment of the City Library.

As the level of funding cuts to the Council has risen from 2010 onwards, the Council has been faced, like many other local authorities, with a fundamentally different scope and level of financial pressures resulting from national reductions in public spending which will continue beyond the next Spending Review. In many ways, the Council has done well to adjust to the exceptional cuts in funding that it has faced in the last two to three years.

**Independent Review of the Financial Position of Birmingham City Council  
INLOGOV, University of Birmingham**

The use of rigid cash limits on service directorates appears to have served the Council well by enabling tactical reductions in expenditure in many services. The Council has avoided large overspends that would have increased the pressure for significant cuts in services above and beyond those that will already be required to meet future funding reductions.

There is now a need, however, to move from a tactical to a strategic approach to ensure that the Council will be able to deliver the expenditure cuts likely to be required in successive financial years before and after the next Spending Review. There is a need for the Council to move towards a more outcome-based perspective in the allocation of its resources. Such a move also presents an opportunity. An outcome-focussed approach will involve new ways of working, with the Council seeking to identify, and to make explicit, planned outcomes which will be delivered through strategic commissioning - including joint and strategic commissioning with the Clinical Commissioning Groups. Such an approach will allow the Council to re-direct resources to priorities, to place more emphasis on seeking flexible approaches to achieve outcomes while controlling and managing risk. In this scenario, financial performance should not be considered in isolation but as part of a bigger picture which examines how well the Council matches its resources to the delivery of holistic and sustainable outcomes. The *Modelling Birmingham* project, led by INLOGOV and delivered through the Public Services Academy, is supporting the realisation of these ambitions.

There are many good examples of local authorities which are moving to outcome focused approaches, working through co-production and achieving long term changes in behaviours and expectations. For example:

- The Swindon *Life Project* breaks the mould of traditional and often ineffective multiple interventions and gives back responsibility over their own lives to families labelled as 'troubled'. This approach has delivered better outcomes for parents and children and significant savings for the council and other agencies.
- In the London Borough of Southwark the *Southwark Circle* demonstrates the contribution that older people can make to their own wellbeing and that of others, preventing decline, promoting independence, combating isolation and keeping people mentally and socially active while making a real contribution to better outcomes for themselves and others.
- In Coventry, the close involvement of the parents of children with profound disabilities has enabled the re-design of their transport service to include coproduction, giving more autonomy and better outcomes for families and significant savings for the council.
- Westminster City Council has developed a 'contract' with citizens which makes explicit what the council can deliver and how it expects its citizens to behave.

- Reading Borough Council's *Transforming Early Years* team aims to reduce the need for expensive downstream intervention with families that need most support. This exercise in "radical efficiency" (Gillinson et al, 2010) involves co-production with an Expert Parent Club and Community Café. Savings of 15 per cent annually over three years are envisaged (NESTA and Innovation Unit, 2012)

These initiatives are part of a significant change in thinking about how local government can manage expectations, reduce dependency on publicly funded services and focus on outcomes. Some of the issues involved in moving to a more outcome focused strategy, while managing demand and harnessing community capacity are explored in more detail in Appendix V.

## Future Risks

This section of the report considers the more significant risks to the Council in achieving service delivery and a satisfactory financial outcome in future years. While this report emphasises financial and accounting matters, the objective is the achievement of better service outcomes for local residents.

## Equal Pay

One of the most significant financial risks facing Birmingham is represented by a major, but difficult to quantify, liability to pay compensation under equal pay claims. It is not known what the impact of future claims and future court decisions will be, but the Council is likely to face requirements to pay very substantial sums. These sums depend upon how many come forward to claim and the validity of their claims.

The sums involved will be impossible to meet out of revenue, and will need to be approved for capitalisation by the Government. Without access to borrowing or other capital resources for future equal pay liabilities the Council will have considerable difficulties in maintaining financial stability. This is the single most important issue on which the Council should lobby the Government. The Government has already approved previous rounds of capitalisation. Repeated rounds of capitalisation may resolve the immediate funding problem but they, in turn, have an ever-increasing impact on revenue year-on-year. A provision of £291.8m has been made in the accounts for year ended March 2011 and "Payments are envisaged in future years but the extent of these cannot be quantified at present" (BCC, 2012a, p8 & p.104). It will be possible for some claims to be lodged through to 2017. The Council will need to re-assess this provision regularly till then.,

## Reserves

In the view of both the City Council's senior finance managers and the external auditor (Audit Commission, 2012a, p. 62), the level of reserves is weak. For example, LGA data at 1<sup>st</sup> April 2012, (Appendix 2) indicates that the level of the Council's non-school reserves, as a percentage of its annual

net revenue expenditure, is the lowest of all of the English metropolitan district authorities (DCLG, 2012a).

This low level of reserves presents a particular risk inherent in the delivery of a savings programme on the scale facing Birmingham City Council.

There is some evidence that the Council is taking steps to build up its usable reserves. General Fund revenue reserves and balances were £90.2m in 2009/10 and £105.4m in 2010/11<sup>2</sup>. The City Council should seek to increase general reserves which would, in principle, be available to use to fund any emergency expenditure. The Council has recognised the need to strengthen its reserves in its review of the impact of the Government's reform of business rates (BCC, 2012e, p.3). The Council's 2012 Business Plan and Budget (BCC, 2012d, p.97) indicates that the only reserve which is not earmarked for specific purposes is the 'Corporate Working Balance' which has planned totals (net of expenditures carried forward) rising from £16.0m in 2011/12 to £25.9m in 2015/16.

What the appropriate level of this general reserve should be is a political decision and we recognise the difficulties of putting money into reserves in a period of severe financial constraint and cuts in services. However, we believe that the planned increase in reserves may be insufficient to reduce the level of future financial risks to an acceptable level. For example, a level of general reserves of only one per cent of annual gross expenditure would put a minimum level of the general reserve at £34m. We therefore recommend that the Council continues its present policy of adding to general reserves each year. To provide the rationale for this approach, the Council should review its policies in respect of the purposes and levels of its reserves and produce a quantified assessment of the reserves needed in line with such policies and seek to establish a process to ensure a medium term progress towards achievement of an appropriate level of reserves.

## **Closing the Funding Gap**

The difficult national financial context, and an examination of Birmingham's thorough internal financial planning work suggest that the City will the need to take steps to bridge an increasing budget gap in coming years. The shortfall of funding against future spending needs presents a major challenge to the Council that needs to be resolved.

The Council has had some success in recent years, adopting tactical approaches to reduce the funding gap that it has faced; based largely upon identifying costs that could be eliminated or reduced within its individual services and support areas. The difficulty that the Council faces is that it is likely to face very challenging and increasing budget gaps over the next five years and beyond. The scale of this future challenge leads us to believe that the Council must take a more strategic approach through a re-appraisal of its priorities. We believe that the Council should decide not only which

---

<sup>2</sup> Communication, Birmingham City Council, September 2012.

**Independent Review of the Financial Position of Birmingham City Council  
INLOGOV, University of Birmingham**

services, delivering which priority outcomes, will take precedence in Council spending, but also clarify explicitly which current services will not have priority status and which will be de-commissioned in the face of the significant budget cuts it faces.

The existing approach, will not be sufficient to enable the Council to take difficult decisions in a strategic way. The ability of individual directorates to achieve and sustain the necessary annual savings to bridge the increasingly-challenging budget gaps that are in prospect must be questioned. It will become increasingly difficult for all expected savings to be backed up by realistic and specific action plans: for example the revenue budget monitoring statement up to 31<sup>st</sup> May 2012 reported that £15.6m of the overall savings target for 2012/13 still required actions to be identified to secure spending reductions. Furthermore, some savings have been met by one-off reductions in previous years and these cannot necessarily be expected to be replicated in future years (BCC 2102f, pp.8-9).

We understand from our interviews that the 'star chamber' process was reasonably effective. The previous cabinet member for Finance was reported to us as having had a determined approach to ensuring that savings were delivered and progress was made, in spite of some savings projections which were not supported by the necessary strategic policy decisions. However, the projected funding gap now requires a process which is more strategic and moves beyond percentage reductions to a focus on allocating resources to the delivery of priority outcomes.

The first stage of cutting, which the Council has been going through, focuses on savings that can be made without having to face up to the big strategic challenges. The extent to which this type of approach can deliver is finite. The scale of challenge the Council faces means that issues must be addressed strategically. Otherwise, in both financial and service terms, the process is likely to fail.

The level of current budget pressures, and the likelihood of a continuing regime of reduced central government support towards local government funding, produces an environment in which the Council must focus on its priority outcomes. This means taking more innovative approaches to service delivery. The Council should assess the relative potential for in-house delivery, the outsourcing of services and the increased involvement of volunteers in co-production. There is also a need to consider the mix of revenue and capital investment to seek long-term reductions in running costs.

The transfer of responsibilities and budgets to districts should be part of this strategic analysis. The Council should seek to distinguish those services in which a city-wide approach will provide a relatively more effective service delivery and the best possible outcomes from those for which a locally-driven district-based approach will maximise savings and provide an acceptable level of service delivery. New mechanisms are being brought in, but there is a risk that the move to the districts-based model of service

delivery will make it harder to achieve savings because of higher transaction costs and the loss of economies of scale.

We understand that a majority of the districts are in deficit in their budgets due to prior year overspends while a few are in surplus. It will be necessary to think constructively about these opening positions. There is little incentive provided to districts which are in deficit by a system of imposing penalties on them with unrealistic expectations of deficit recovery. However the Council will also need to develop procedures to ensure that future financial deficits are avoided as far as possible and to give those districts currently in surplus some benefit arising from their prior financial performance. Encouraging districts to plan in terms of service outcomes and to promote learning between districts including member and officer cross-district support arrangements and peer review across districts will assist achievement of both financial and service objectives.

The political leadership of the districts and their effectiveness in engaging local people about difficult choices and harnessing local capacity will be crucial to the success of the move to a district model. INLOGOV will be providing pro bono advice and support to the City Council on the development of the district model.

## **Borrowing**

The level of borrowing, net of short term investments, by the Council had risen to a comparatively high level – £2,329m at 31 March 2011. However, the auditor was ‘satisfied that the level of borrowing is not currently a threat to the Council’s financial resilience’ (Audit Commission, 2011, p.16-17). The strength of the Council’s liquidity and treasury management processes have been commented upon in two recent reports from rating agencies (Standard and Poor, 2011; Moody’s 2012). The Council did not breach any of its prudential borrowing limits in 2011/12 (BCC, 2012g).

We understand that net borrowing has increased by a further £452m in the year to 31 March 2012 (BCC 2012g). The increase is largely accounted for by the removal of Housing Revenue Account (HRA) subsidy which has resulted in new borrowings of £336m for the Council. It may be possible for the Council to build more homes and borrow against future rental income, although the Council has indicated a concern that, like some other local authorities, it will have the maximum level of loans under the HRA reforms and will not be able to generate more funding for new housing in the short-term (CLG Committee, 2012, par. 91).

There are also current, and potentially future, capitalisations of equal pay liabilities together with payment obligations of PFI and similar transactions.

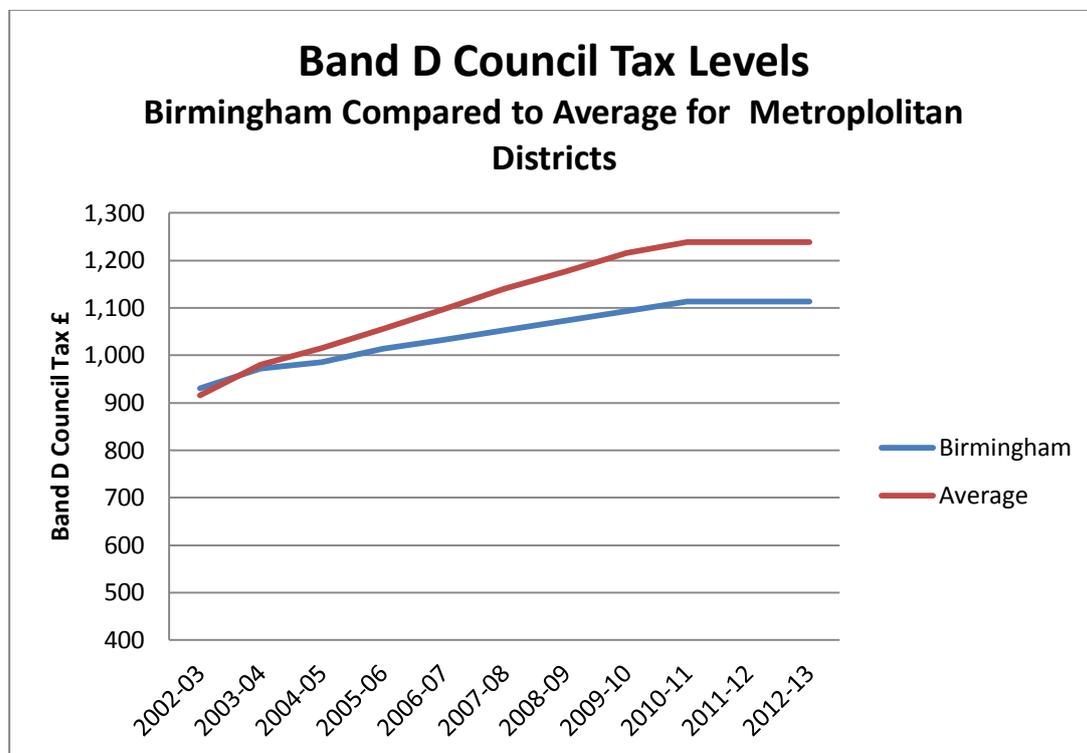
All these commitments contribute to reducing the Council’s room for discretion. There is a related ‘leveraging effect’ in that fixed commitments to cover interest and repay borrowings have the effect of increasing the burden of cuts on other elements of expenditure above the headline percentage of

reduced support from central government. The Council has a repayment programme built into its Long-Term Financial Plan which aims to reduce outstanding debt in relation to historic borrowing, but we believe that the Council should take care that new borrowing does not undermine its goal of reducing leverage.

## Income from Council Tax

In our introduction we commented on the Council's decision not to raise council tax. Figure 4 shows that Birmingham has increased council tax less rapidly than the average metropolitan district. Although this is a political decision, it does appear as though a rise in council tax should at least be considered as a way of maximising income and offsetting the reductions in central government funding, in the medium term, if not in the short term.

Figure 4: Comparative Council Tax Levels



## Council Tax Benefit

Council tax benefit localisation is a very immediate issue – there will be a reduction in resources available to the Council and the new system must be in place by the beginning of the next financial year 2013/14. The parameters for payment of council tax benefit to pensioners will be determined by a national framework, but each local authority will be able to set its own parameters for council tax benefit eligibility for working age residents.

There are various options on how the criteria for residents to claim benefit might be adjusted to deliver the necessary savings and these are currently being considered by the Council. One option is to continue with current

criteria for a year (through 2013/14). An analysis of the cost of this approach to the Council indicates that 'The reduction in the grant allowance will need to be supplemented by the Council by approximately £10 million' (BCC, 2012b, p.5).

Other options include placing a cap on payments for working age recipients to 80, 75 or 70 per cent of their council tax charge or increasing the taper on the applicants' excess income in order to reduce the cost of the benefit to the Council. These options will either place pressure on vulnerable local residents or the Council's finances or, as is likely, both. Policies on council tax benefit and housing policies should be integrated as there is a real danger that the aggressive pursuit of savings in council tax benefits could have a detrimental impact on budgets in other parts of the City Council – for example, around homelessness or social care budgets. The strategy adopted for responding to the localisation of council tax support should be framed taking account of its consequences across the Council and the city as a whole.

## **Business Rates Retention**

The Chief Executive, Stephen Hughes is on the government's Local Government Finance Working Group which is responsible for detailed issues in the design of the business rates retention system and will therefore be in an excellent position to pick up early warnings of any risks in the scheme for Birmingham City Council, and also be able to draw attention to such problems in consultations about the design of the scheme.

It is important that, in formulating its economic development policies, Birmingham recognises the potential contribution of these policies to future income streams within the City Council. The Council's "Narrowing the Gap" policy is important in this respect and we believe that it is a priority that the Council has an explicit strategy for business rates maximisation.

The Technical Consultation on Business Rates Retention, launched by CLG on the 17<sup>th</sup> July 2012 (DCLG, 2012b), contains a disconcerting element for Birmingham. It proposes a number of changes to the Formula Grant distribution formula to move more money to sparsely populated areas although the likely cost to Birmingham will be limited by the floor damping mechanism. It is clearly in the interests of the City Council to continue to lobby vigorously against this change, both individually and through the Special Interest Group of Metropolitan Authorities (SIGOMA).

## **Accounting Issues**

There have been a number of issues with the Council's accounts which stretch back over some years. The accounts were qualified by the auditor in 2008/09 due to problems in accounting for fixed assets.

In 2010/11 there were still problems with the accounts, which are in the process of being resolved. Although the audit report was unqualified with

**Independent Review of the Financial Position of Birmingham City Council  
INLOGOV, University of Birmingham**

regard to these matters, the Annual Governance Report (Audit Commission, 2012) was highly critical.

The Council has a very large asset base and International Financial Reporting Standards (IFRS) have introduced new requirements which have been difficult to accommodate given the large number of Council leases and complexities in accounting for PFI (Audit Commission 2012, p. 9).

The Council's SAP system does not produce IFRS compliant accounts for the General Ledger so that a great deal of extra work involving interim solutions using spreadsheets was required in 2010/11 to achieve compliance. To solve this problem for future years, the SAP system needs fundamental reconfiguration so that IFRS compliant accounts are produced without the need for significant manual intervention, and this improvement is being implemented. There have also been particular and significant problems with accounting for debtors and creditors (Audit Commission 2012, p. 14).

These issues delayed completion of the 2010/11 financial statements (Audit Commission 2012, p. 9). The Council identified many of the accounting issues to the Auditor, on which the Auditor subsequently reported and most, but not all, of the problems have related to non-cash transactions rather than issues which affect the actual resources available.

It is difficult to be certain about the root causes of these significant problems, which were known about, but not resolved for a number of years. We understand that the production of the annual accounts was not integrated fully with other aspects of the Council's day-to-day financial administration. A more effective structure would be to place those sections involved in day-to-day financial administration in positions of responsibility for the work needed to produce the annual accounts. This might have an added benefit of improving the availability and understanding of financial information used for in-year financial reporting. This legacy of problems has been taken very seriously by the Council – some members of the finance team that ran these systems have left the authority and the finance team has been restructured and staff moved to new roles in order to strengthen the team. There is an improvement plan (Audit Committee 2012a) in place that addresses the recommendations for remedial action in the Annual Governance Report (Audit Commission, 2012) and there have been two progress reports so far this year (Audit Committee b,c). Details are contained in an action plan written with PWC. A considerable amount of work is required to deliver this action plan and it will be impressive if it can all be completed to the planned schedule.

The difficulties which have arisen in producing the year-end accounts need to be considered in the context of their impact on regular financial reporting within the Council. However, the auditor has reported that 'in general, the quality of in-year financial reporting is good' (Audit Commission, 2011, p 17)). We believe that the Council is making progress in resolving the serious problems it has had with accounting. It appears likely that the historic problems relating to the Council's accounts will be successfully resolved, but

this issue should remain a priority and progress on plans should be kept under constant review by both senior officers and the Cabinet. Failure to rectify the problems, coupled with further adverse audit reports, will inevitably damage external perceptions of the quality of the City Council's financial management.

## **The Role of Members in Financial Management**

INLOGOV is currently researching the changing role of members and looking at the political leadership skills and capacity which will be needed by councils facing a very challenging future. Early findings suggest that although members cope very well with the demands of their roles, many do not consider themselves to be sufficiently well developed or supported to play their roles in that future as effectively as possible.

The decisions which the Council needs to take in both the short and medium term are complex and challenging to an unprecedented degree. As a new administration it is essential that all members, and particularly those chairing district committees, portfolio holders and scrutiny chairs receive the development support they need.

## **Recommendations**

This review of the financial position of Birmingham City Council has highlighted a number of critical issues facing the Council over the next five to ten years. These include the cost of equal pay claims, the need to plan to build up reserves and reduce borrowings, accounting issues and the impact of recent and proposed central government policy changes such as council tax reform and business rates retention.

Many of the issues and necessary responses reach beyond the technical issues of financial management into the particular culture, structures and systems that exist in the Council.

Many impacts of the changing environment, in one form or another, confront all local authorities and may be particularly acute within the core cities. We therefore recommend that the Council continues to work with other core cities and large urban authorities to ensure that central government is aware of the depth and complexity of issues that are faced by local governments and their citizens.

We recommend the Council to focus on outcomes, rather than service maintenance, for the strategic underpinning of its savings plans. The cuts in expenditure required in the next ten years to balance the financial position of the Council can only be achieved by seeking to integrate the activities of the Council, both internally and by working with external organisations. This points us towards the need for the Council to achieve certain changes, in both political and managerial spheres, and to seek to minimise any tendency for decisions to be made as short-term financial fixes resulting in

uncoordinated service cuts. Such changes require a period of at least ten years, with a focus beyond the next local government elections. .

We appreciate that such a change of emphasis and approach will not be easy. However, the Council has achieved some success to date in controlling expenditure in an environment which has involved significant cuts in its financial resources. The Council's debt levels, although high, are not so severe currently as to cast doubt on the financial resilience of the Council's core services. The Leader's Policy Statement (Bore, 2012) may provide a suitable starting point to enable the development of the Council's outcome-based strategies.

## **Detailed recommendations**

Some detailed recommendations are listed below. These should be seen in both political and managerial contexts. They are political in the context that they require the members of the Council to support the executive officers and to develop specific areas to lobby for additional support, either working with other core cities or urban authorities or, where necessary, to ensure that decision makers are aware of the particular set of circumstances affecting the City of Birmingham. They are managerial in the context that detailed operational plans need to be developed and implemented from an agreed set of strategic policies. The executive officers of the Council must feel able to provide an open and balanced view to members of progress towards the achievement of stated objectives and that they will have the support of members to implement what may be difficult, and at times unpopular, decisions.

### **Specific recommendations:**

1. Recognising the particularly challenging environment that the Council faces over the next five to ten years, that the Council adopts a strategic response to the issues it faces.
2. Develop a strategy for the commissioning and provision of services based upon a planned outcomes and explicit indications of priority services and those that will not have priority during the period in which financial resources are constrained. Savings targets should be integrated into the outcomes-based approach.
3. Identify particular issues for the development of a strategy for lobbying of assistance and freedom of action from central government and adopt this approach as a routine part of risk management processes. Current issues might include:
  - a. Capitalisation of expenditure on equal pay;
  - b. Localisation of council tax benefits;
  - c. Business rates retention;

**Independent Review of the Financial Position of Birmingham City Council  
INLOGOV, University of Birmingham**

- d. Housing benefit reform and freedom to borrow secured on social housing rents.
4. A key element of a more strategic approach will be the Council's response to the funding gap it faces. We recommend that the Council builds on the 'star chamber' approach to make the savings process more strategically focused by seeking to identify the real service priorities of the Council, interviewing both officers and members – using a process more akin to a select committee.
5. We believe that the Council should set at least a ten-year timescale for the build-up of reserves and a gradual reduction in borrowing levels to specified targets. In view of the restriction on future policy choice that the level of borrowing is already imposing on the revenue account the Council should take care that new borrowing does not undermine its ten year plan for borrowing levels.
6. Policies on council tax benefit and housing policies should be integrated in view of the danger that savings in council tax benefits could have a detrimental impact on budgets in other parts of the Council such as homelessness or social care budgets.
7. The Council is making progress in resolving the serious problems it has had with accounting. This process should remain a priority and progress on plans should be kept under constant review by both senior officers and the Cabinet.
8. The Council should consider its relationship the public it serves. Any policy option involving restriction of services will unavoidably be politically contentious but the negative impact could be reduced by having a more engaging and communicative approach. The development of a district-led model for some services provides a potential for a locally-led engagement and we encourage the Council to continue to support this model. It will be necessary to determine which services are best controlled and operated centrally in contrast with those which benefit from local management and flexibility. Furthermore, particularly in times of financial austerity, a decentralised approach requires a clear understanding on the limits of local financial authority and would benefit from a common expectation between the districts and the central council of the requirements for recovery of financial deficits and the provision of incentives to districts through an equitable sharing of financial surpluses.

## Appendix I: References

Audit Commission (2011), Annual Audit Letter, Birmingham City Council Audit 2010/11.

Audit Commission (2012), Annual Governance Report, Birmingham City Council Audit 2010/11.

Audit Committee (2012a), Final Accounts Improvement Plan 2011/12 and Beyond, 24 January

Audit Committee (2012b), Final Accounts Improvement Plan 2011/12 and Beyond, 20 March

Audit Committee (2012c), Final Accounts Improvement Plan 2011/12 and Beyond, 26 June

BCC (2012a), Statement of Accounts 2010/11, Birmingham City Council, 20 March.

BCC (2012b), Localisation of Council Tax Support, High Level Options Briefing Note, 8 March.

BCC (2012c), Corporate Revenue Budget Monitoring 2011/12 - Month 11.

BCC (2012d), Council Business Plan and Budget 2012+

BCC (2012e), Local Government Resource Review Update, 19 May.

BCC (2012f), Corporate Revenue Budget Monitoring 2012/13 – Month 2

BCC (2012g), Treasury Management Outturn Report, 31 July.

Bore, Sir Albert (2012) Leader's Policy Statement, Birmingham City Council, 12 June.

CLG Committee (2012), Financing of New Housing Supply, House of Commons Communities and Local Government Committee, HC 1652.

DCLG (2012a), Local authority revenue expenditure and financing 2012-13 individual local authority data, Department for Communities and Local Government, <http://www.communities.gov.uk/publications/corporate/statistics/revenuelocaldatabudget201213>.

DCLG (2012b) Business Rates Retention: Technical consultation, Department for Communities and Local Government, July, <http://www.communities.gov.uk/publications/localgovernment/businessratestechnical>

**Independent Review of the Financial Position of Birmingham City Council  
INLOGOV, University of Birmingham**

Gillinson, S. Horne, M. and Baeck P. (2010) Radical Efficiency: Different, better, lower cost public services Innovation Unit and NESTA,.

HM Treasury (2012), Budget, Annex A, March, [http://cdn.hm-treasury.gov.uk/budget2012\\_annexa.pdf](http://cdn.hm-treasury.gov.uk/budget2012_annexa.pdf)

IFS (2012) The IFS Green Budget February. Institute for Fiscal Studies, February, <http://www.ifs.org.uk/budgets/gb2012/gb2012.pdf>

LGA (2012) Funding Outlook for councils from 2010/11 to 2019/20, Local Government Association, June.

Moody's Investor Services (2012), Credit opinion; Birmingham City Council' 17<sup>th</sup> February.

NESTA and Innovation Unit (2012) Transforming Early Years- Radical Efficiency in Practice: Families Taking Control in Reading, <http://www.nesta.org.uk/library/documents/TEYVisualCaseStudyReading.pdf>

OBR (2012), Fiscal Sustainability Report, Office for Budget Responsibility, July

Standard and Poor's Global Credit Portal (2011), Research Update; Birmingham City Council is Assigned 'AA+' Rating on Positive Liquidity; Outlook Stable, 11 October.

## Appendix II: Metropolitan Districts' Non-School Reserves

### Metropolitan Estimated Non-School Reserves at 1st April 2012

| Local authority | NET REVENUE<br>EXPENDITURE<br>(£000) | EARMARKED<br>RESERVES<br>(£000) | UNALLOCATED<br>RESERVES<br>(£000) | TOTAL<br>RESERVES<br>(£000) | Reserves as<br>% of net<br>expenditure |
|-----------------|--------------------------------------|---------------------------------|-----------------------------------|-----------------------------|--|
| Birmingham      | 960,722                              | 45,300                          | 19,900                            | 65,200                      | 6.8                                    |
| Gateshead       | 187,706                              | 9,465                           | 3,994                             | 13,459                      | 7.2                                    |
| Leeds           | 579,777                              | 25,928                          | 19,237                            | 45,165                      | 7.8                                    |
| Sandwell        | 277,978                              | 11,323                          | 13,400                            | 24,723                      | 8.9                                    |
| Rochdale        | 191,743                              | 17,637                          | 5                                 | 17,642                      | 9.2                                    |
| Coventry        | 264,406                              | 20,999                          | 4,232                             | 25,231                      | 9.5                                    |
| Salford         | 222,658                              | 10,471                          | 11,883                            | 22,354                      | 10.0                                   |
| Sheffield       | 466,902                              | 41,677                          | 10,887                            | 52,564                      | 11.3                                   |
| Newcastle       | 265,515                              | 20,813                          | 10,134                            | 30,947                      | 11.7                                   |
| Sefton          | 249,158                              | 21,066                          | 8,573                             | 29,639                      | 11.9                                   |
| Walsall         | 240,052                              | 16,131                          | 13,748                            | 29,879                      | 12.4                                   |
| Rotherham       | 213,222                              | 20,750                          | 6,002                             | 26,752                      | 12.5                                   |
| Trafford        | 159,333                              | 11,382                          | 8,665                             | 20,047                      | 12.6                                   |
| North Tyneside  | 169,041                              | 17,608                          | 6,604                             | 24,212                      | 14.3                                   |
| Doncaster       | 237,430                              | 26,741                          | 7,429                             | 34,170                      | 14.4                                   |
| Stockport       | 218,629                              | 24,128                          | 8,493                             | 32,621                      | 14.9                                   |
| Bury            | 138,696                              | 16,635                          | 6,805                             | 23,440                      | 16.9                                   |
| South Tyneside  | 143,112                              | 23,629                          | 1,500                             | 25,129                      | 17.6                                   |
| Dudley          | 237,552                              | 33,358                          | 11,100                            | 44,458                      | 18.7                                   |
| Liverpool       | 483,984                              | 79,948                          | 16,000                            | 95,948                      | 19.8                                   |
| Oldham          | 206,360                              | 26,574                          | 15,650                            | 42,224                      | 20.5                                   |
| Tameside        | 191,699                              | 19,464                          | 21,330                            | 40,794                      | 21.3                                   |
| Wirral          | 291,995                              | 44,696                          | 18,405                            | 63,101                      | 21.6                                   |
| Bradford        | 426,780                              | 82,800                          | 10,803                            | 93,603                      | 21.9                                   |
| Wakefield       | 245,299                              | 49,320                          | 6,673                             | 55,993                      | 22.8                                   |
| Wigan           | 231,133                              | 44,473                          | 9,828                             | 54,301                      | 23.5                                   |
| Kirklees        | 317,136                              | 53,607                          | 21,866                            | 75,473                      | 23.8                                   |
| Knowsley        | 164,292                              | 38,022                          | 5,270                             | 43,292                      | 26.4                                   |
| Solihull        | 148,631                              | 28,209                          | 11,846                            | 40,055                      | 26.9                                   |
| Calderdale      | 152,598                              | 36,484                          | 6,778                             | 43,262                      | 28.4                                   |
| St Helens       | 149,779                              | 30,244                          | 13,471                            | 43,715                      | 29.2                                   |
| Barnsley        | 253,852                              | 64,526                          | 10,000                            | 74,526                      | 29.4                                   |
| Manchester      | 497,925                              | 123,308                         | 23,743                            | 147,051                     | 29.5                                   |
| Sunderland      | 275,252                              | 87,941                          | 7,570                             | 95,511                      | 34.7                                   |
| Wolverhampton   | 232,703                              | 41,171                          | 43,062                            | 84,233                      | 36.2                                   |
| Bolton          | 216,343                              | 75,921                          | 8,400                             | 84,321                      | 39.0                                   |

**Independent Review of the Financial Position of Birmingham City Council  
INLOGOV, University of Birmingham**

### Appendix III: Documents Reviewed

Financial position up to 2010/11, including the Outturn and Final Accounts for that year  
External Audit reports  
The 2011/12 Financial Monitoring position and the Outturn position  
The Business Plan 2012+ and Budget, including our Long Term Financial Strategy  
The early financial monitoring position for 2012/13  
Briefings to the Administration on the developing financial position  
The Council's risk assessments  
Latest and anticipated developments in local government finance and their potential impact on the Council  
Appendix 1 Final 2010-11.pdf  
Appendix 2 Final 2010-11.pdf  
Appendix 4 Final 2010-11.pdf  
Capital Outturn 2010-11 Chapter 2.pdf  
Collection Fund Chapter 5.pdf  
Final Accounts cover report.pdf  
HRA Financial Commentary Chapter 4.pdf  
Month 1 2012-13 - Note for Cllr Ward 18Jun12.doc  
Annual Audit Letter BCC Audit Committee 20 Dec2011.pdf  
Annual Governance Report 2010-2011- FINAL[1].pdf  
Audit Committee 200312 AGR FINAL[1].pdf  
Audit Committee 200312 Statement of Accounts 2010-11 [1].pdf  
Budget Book 2010-11 [1].pdf  
Budget Book 2011-12 [1].pdf  
Budget Book 2012-13 [1].pdf  
Business Plan and Budget 2012+ with cover.pdf  
Cabinet Report Qtr 1 Capital 11-12[1].pdf  
Cabinet Report Qtr 2 Capital 11-12 nov 21+[1].pdf  
Cabinet Report Qtr 3 Capital 1112 final[1].pdf  
Corporate Revenue Budget Monitoring 2011-12 Month 2 - FINAL[2].pdf  
Corporate Revenue Budget Monitoring 2011-12 Month 3 & 4 final [1].pdf  
Corporate Revenue Budget Monitoring2011-12 Month 5 [1].pdf  
Corporate Revenue Budget Monitoring 2011-12 Month 6 (1).pdf  
Corporate Revenue Budget Monitoring 2011-12 Month 7 [1].pdf  
Corporate Revenue Budget Monitoring 2011-12 Month 8 [1].pdf  
Corporate Revenue Budget Monitoring 2011-12 Month 8(2) Additional info.pdf  
Corporate Revenue Budget Monitoring 2011-12 Month 9 & 10.pdf  
Corporate Revenue Budget Monitoring 2011-12 Month 11 - Final[1].pdf  
Corporate Risk Reg Update for March12.pdf  
Folder contents.doc  
Leader briefing 25.05.12.doc  
Letter of Representation 2010-11 FINAL[1].pdf  
Local Government Resource Review Update BriefingFINAL.doc  
Audit committee 20th March Improvement Plan FINAL 1.pdf  
Audit committee June Improvement Plan final.pdf  
Jan Audit Committee - final accounts improvement programme.pdf  
Council Business Plan 2011+.pdf  
D1148 - EMT Cover report re Replacement Council Tax Benefit.doc  
EG023 - LOCALISATION OF COUNCIL TAX BENEFIT -Options paper v.3.doc  
EMT Awayday June 2012 contents.pdf)

**Independent Review of the Financial Position of Birmingham City Council  
INLOGOV, University of Birmingham**

Section 3 Finance

Cover note savings and pressures.doc

Paper 3a.xls Paper 3b.xls: Paper 3c.xls)

Budget Book 2013 v2 280312 WOC new directorates wp4.xls)

Executive briefing on Capital 11-6-12.doc

The level and sustainability of Council Borrowing Scrutiny16-12-11final[1].pdf

(See attached file: Credit Opinion - Birmingham City Council.pdf)(See attached file: S&P

Research update press release BCC.pdf)

Financial Outturn Report

Cabinet Report.doc, Cabinet Report App1.doc, Cabinet Report App2.doc

Cabinet Report App3.doc, Cabinet report App4.doc, Cabinet Report App5.doc)

Monitoring report on final accounts

Final Accounts Redraft (02).mpp:

Final Accounts Redraft (02).pdf,

SummaryPLan 0731.xls

## **Appendix IV: Interviewees**

Sir Albert Bore, Leader of Birmingham City Council

Stephen Hughes, Chief Executive, BCC

Paul Dransfield, Strategic Director of Corporate Resources

John Warlow, Director of Finance

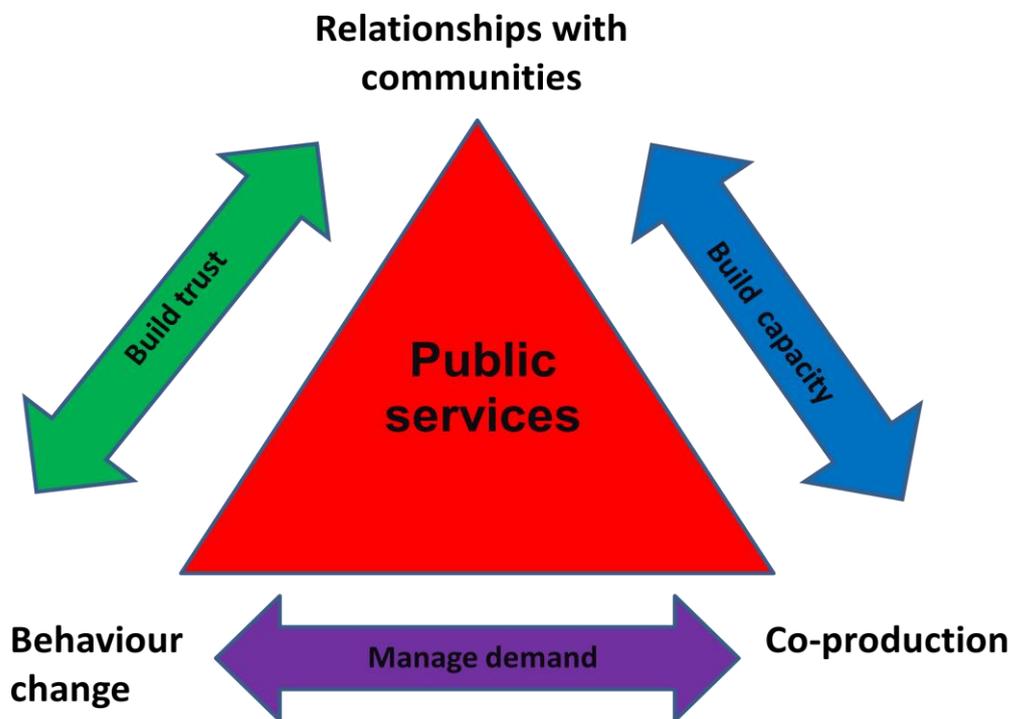
Steve Powell, Assistant Director of Financial Strategy

Mark Stocks, District Auditor

## Appendix V: Developing a New Model for Public Services

INLOGOV is currently drawing together research on some of the major themes in local public services to construct a unifying model, within which councils can explore how they need to change themselves and their relationships with citizens in order to meet the challenges of rising demand and reducing resources. The Barnett 'graph of doom' applies to all upper tier authorities and it is clear that the strategies which have worked in the past, such as incremental savings and internal re-organisations will not deliver savings of the order of magnitude needed to close the gap. That suggests that other ways of closing the gap are needed. Figure 1 below illustrates the main features of the model.

**Figure 1: A new model of public services for a time of austerity**



There are a number of key issues to be tackled in closing the gap and moving to a strategic, outcome based approach to the allocation of scarce resources:

### Building Stronger Relationships with Residents

Relationship with residents will need to be based on mutual trust and it will be necessary to have some difficult discussions about what the Council can do for residents and what they will need to do for themselves and others. Effective engagement, particularly through ward members and district committees is an essential part of building that trust. Changes in attitudes

and mutual expectations will be necessary and one way of achieving that change is to begin to focus on people's capacity as well as on their needs.

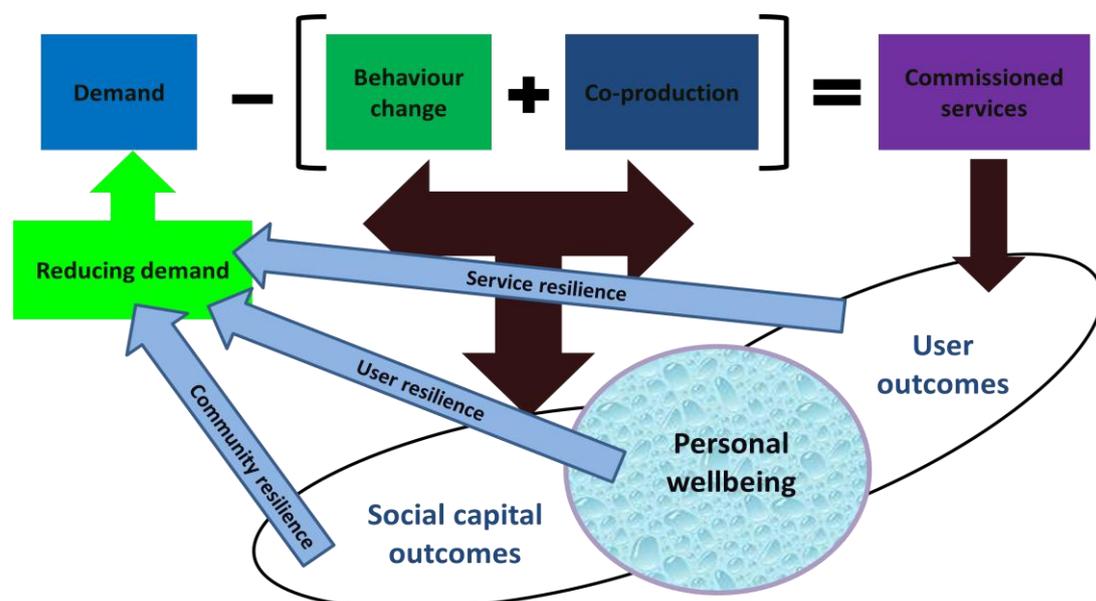
## Co-production

Co-production is not a new concept. Individuals and communities already co-produce many outcomes, for example, as school governors, as volunteers and as carers. As resources are likely to become increasingly scarce it is essential to harness the capacity of residents who are able to do more for themselves and others to do so. Many councils are transferring the management of assets, such as community centres, to local residents. By increasing involvement, through leisure trusts and volunteering, for example in libraries, art galleries and museums, children's services and adult social care it is possible for councils to reduce cost and build capacity in services and communities.

## Behaviour change

Behaviour change is also not a new concept, although there is often a lack of understanding on the part of policy makers about what works. The use of inappropriate levers for change, for example, criticising of 'bad' behaviour rather than recognising and rewarding 'good' behaviour has brought behaviour change, as an approach which can help reduce demand into disrepute. However, there is wealth of evidence about the impact sustained behaviour change can have on reducing the costs of and demand for public services which the Council and its health partners can draw on. Figure 2 below shows how co-production and behaviour change can be used to reconcile council-provided resources with demand.

Figure 2: Changing the equation



**Independent Review of the Financial Position of Birmingham City Council  
INLOGOV, University of Birmingham**

It is clear that there will always be services which the Council has to deliver or commission, to protect the vulnerable, promote the health and wellbeing of the whole population and enforce the law. However, co-production and behaviour change can help reduce the volume and cost of the services which do need to be commissioned. By supporting co-production and behaviour change and by commissioning holistically and strategically, the Council can reduce waste and duplication of effort and ensure a better focus on outcomes. All councils struggle with commissioning for a number of complex reasons. These include the need for outcomes to be holistic while resources are usually allocated to departmental budgets which can reinforce competitive organisational behaviour and silo thinking. In the future councils will need to be more nimble and flexible if they are to be able to make the best use of their limited resources.

UNIVERSITY OF  
BIRMINGHAM

**Birmingham Business School**  
**Institute of Local Government Studies**  
University of Birmingham, Edgbaston, Birmingham B15 2TT

**[www.birmingham.ac.uk/business](http://www.birmingham.ac.uk/business)**  
**[www.birmingham.ac.uk/inlogov](http://www.birmingham.ac.uk/inlogov)**