

Cyngor Sir CEREDIGION County Council

REPORT TO: Governance and Audit Committee

DATE: 19 January 2022

LOCATION: Remotely via Video Conference

TITLE: Report on Audit Wales Financial Sustainability Report 2020-21 and Report on Financial Sustainability of Local Government - Covid-19 Impact, Recovery and Future Challenges

PURPOSE OF REPORT: To update the Governance and Audit Committee regarding the outcome of the 2020-21 Audit Wales Financial Sustainability Assessment of the Council and Audit Wales Report on Financial Sustainability of Local Government

For: Decision

Cabinet Portfolio and Cabinet Member: Cllr. Ray Quant, Deputy Leader of the Council and Cabinet Member for Legal & Governance, People and Organisation, and Democratic Services

BACKGROUND:

Audit Wales has published its 2020-2021 Financial Sustainability Assessment – Ceredigion County Council 2020-2021 (see **Appendix 1**).

A Council Response Form has also been provided by Audit Wales requesting for the relevant section to be completed and returned to them setting out how the Council intends to address the proposal for improvement.

The Council Response Form has been completed and is attached (see **Appendix 2**).

Audit Wales has also published a National Report entitled Financial Sustainability of Local Government – COVID-19 Impact, Recovery and Future Challenges ('the National Report') (see **Appendix 3**).

CURRENT POSITION:

It is understood that Audit Wales shall present its 2020-2021 Financial Sustainability Assessment for Ceredigion County Council (see **Appendix 1**) to the Governance and Audit Committee ('the Committee') today and, as recommended by Audit Wales, this Report setting out the Council's updated position is hereby presented to the Committee.

The Committee is also requested to note and consider the '*Four steps to help with councils' financial sustainability*' in Exhibit 6 of the National Report (see **Appendix 3**) and make any

appropriate recommendations or response to Audit Wales.

RECOMMENDATIONS:

It is recommended that the Committee:

1. Notes the contents of the Audit Wales Financial Sustainability Assessment – Ceredigion County Council 2020-21 (at **Appendix 1**), considers the Council Response Form (at **Appendix 2**) and makes appropriate recommendations; and
2. Notes the National Report (at **Appendix 3**), makes any appropriate recommendations and/or provide a response to Audit Wales

REASON FOR RECOMMENDATIONS:

To keep the Governance and Audit Committee informed of reports, proposals and work being undertaken by Audit Wales and the Council's response.

Appendices:

Appendix 1 – Audit Wales 2020-21 Financial Sustainability Assessment for Ceredigion County Council

Appendix 2 – Council Response Form

Appendix 3 – Audit Wales National Report - Financial Sustainability of Local Government – COVID-19 Impact, Recovery and Future Challenges

Head of Service:

Elin Prysor, Corporate Lead Officer – Legal & Governance Services / Monitoring Officer

Reporting Officer:

Elin Prysor

Date:

20/12/2022

Financial Sustainability Assessment – Ceredigion County Council

Audit year: 2020-21

Month/Year issued: June 2021

Document reference: 2464A2021-22

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Mae'r ddogfen hon hefyd ar gael yn Gymraeg. This document is also available in Welsh.

Contents

The Council remains financially stable and is focussed on future challenges.	
What we looked at and why	4
Proposal for improvement	5
The Council remains financially stable and is focussed on future challenges	6
The immediate impact of COVID-19 on the Council's financial sustainability has been assisted by additional Welsh Government funding	6
The Council has a clear financial strategy over the medium term	7
The Council has continued its record of not making unplanned use of reserves to fund revenue expenditure, and usable reserves have increased in recent years	9
The Council has a good track record of meeting its overall annual budget although there continues to be significant overspends in Social Care	11
The Council has a good track record of meeting savings targets, however, delivering the required savings will be more challenging going forward	12
The Council has maintained favourable liquidity levels over recent years	14

What we looked at and why

- 1 We undertook this assessment as financial sustainability continues to be a risk to councils putting in place proper arrangements to secure value for money in the use of resources. In part, this was informed by the experiences of some councils in England, our knowledge of the financial situation in councils in Wales, and the general trend of decreasing resources for local government combined with rising demand for some services. We undertook a similar project in 2019-20, before the COVID-19 pandemic.
- 2 Our 2020-21 assessment on councils' financial sustainability was in two phases. Phase 1 was a baseline assessment of the initial impact of COVID-19 on local councils' financial position. Phase 1 drew on: the year-end position for 2019-20; the position at the end of quarter 1 for 2020-21; and projections for quarter 2 for 2020-21. Following Phase 1, in October 2020 we published a national summary report – **Financial Sustainability of Local Government as a result of the COVID-19 Pandemic**¹. We found that councils and the Welsh Government have worked well together to mitigate the impact of the pandemic to date, but the future sustainability of the sector is an ongoing challenge.
- 3 The pandemic has had an immediate and profound effect on public sector finances as a whole and, as a consequence, on councils' financial position. The summary report set a high-level baseline position, including the reserves position of local councils before the pandemic. It also set out the initial financial implications of the pandemic for local councils and the scale of the anticipated challenge going forward.
- 4 This report concludes phase 2 of our financial sustainability assessment work during 2020-21. As part of this we are producing a local report for each of the 22 principal councils in Wales.
- 5 We undertook this assessment during January 2021 to March 2021.

¹ [Audit Wales, Financial Sustainability of Local Government as a Result of the COVID-19 Pandemic, October 2020.](#)

Proposal for improvement

Exhibit 1: proposal for improvement

The table below sets out the proposal for improvement that we have identified following this review.

Proposal for improvement

Proposal for improvement

P1 To ensure the Council meets its future financial challenges, the Council should:

- continue to monitor the significant overspends in Social Care; and
- ensure that the Social Services Transformation Project is driving improvement.

The Council remains financially stable and is focussed on future challenges

The immediate impact of COVID-19 on the Council's financial sustainability has been assisted by additional Welsh Government funding

7 This section sets out the impact that COVID-19 has had to date on the Council's financial position and the extent to which this has been mitigated by additional funding from the Welsh Government.

8 We found that:

- the Council has managed the costs of COVID-19 on a Council-wide basis, so that individual services are not in a position where they either 'gain' or 'lose' significantly as a direct result of the financial consequences of COVID-19.
- in 2020-21, the Council initially earmarked a reserve of £1.6 million from existing resources to meet the potential cost of COVID-19. However, the Council is not anticipating using this reserve in 2020-21 because the Welsh Government has met the majority of COVID-19 additional costs to date and additional savings estimated at £1.1 million have been achieved as a result of reduced running costs in providing some services.
- as shown in **Exhibit 1**, the Council has so far received funding of £12.9 million from the Welsh Government for hardship costs, Council Tax Reduction Scheme pressures and loss of income. Total costs net of savings achieved are estimated to be £13.2 million. Whilst Council Tax collection rates suffered earlier in the financial year, they have since improved and the Council expects that any losses at the year-end will be minimal.
- additional funding has also been received from HMRC, the Health Board and a number of other miscellaneous grants are also expected by the year-end in 2020-21.
- as part of its budget setting for 2021-22, the Council has retained a reserve of £1 million in earmarked reserves to cover a potential shortfall in COVID-19 funding going forward. Any surplus income received over and above expenditure will be transferred to earmarked reserves.
- the Council acknowledges there will be a longer-term impact of the COVID-19 pandemic on its overall strategy, the way it provides services and its financial position.

Exhibit 2: the cost to the Council of COVID -19 over 2020-21

The table below shows the Council's estimated additional expenditure and lost income over 2020-21 as a result of COVID-19, and how much of this was mitigated by extra funding from the Welsh Government and expected savings due to the operational impact of COVID-19 on service provision.

The additional amount the Council estimates it will have spent as a result of COVID-19 over 2020-21.	£(8.7) million
The amount of income the Council estimates it will have lost as a result of COVID-19 over 2020-21.	£(5.6) million
Estimated savings achieved due to the operational impact of COVID-19 on service provision	£1.1 million
The amount of additional funding the Council estimates it will receive from the Welsh Government over 2020-21 to mitigate the impact of COVID-19.	£12.9 million
The estimated cost to the Council of COVID-19 over 2020-21 after extra funding from the Welsh Government is taken into account.	£(0.3) million

Source: information provided by Ceredigion County Council

The Council has a clear financial strategy over the medium term

Why strategic financial planning is important

9 A clear and robust financial strategy is important to identify the likely level of funding available to a council, as well as the anticipated level of demand for, and cost of, providing services. Given the recent and anticipated funding pressures facing all councils, it is important to identify how the Council intends to respond to those pressures and how it is planning to meet projected funding gaps.

We found that:

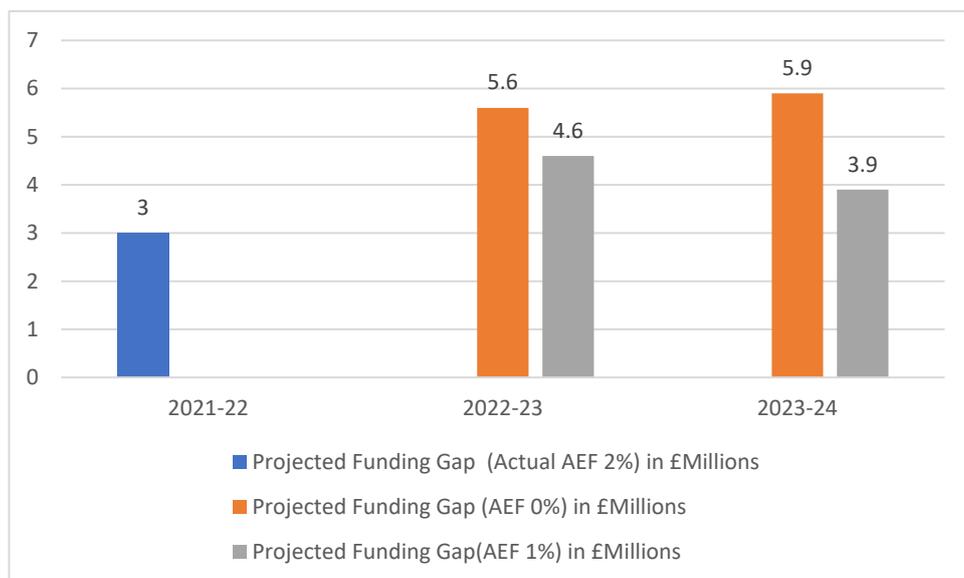
- the Council's Medium Term Financial Plan (MTFP) 2021-22 to 2023-24 supports financial sustainability by identifying key financial challenges,

expected funding gaps and an assessment of how to fund these gaps over the next three years.

- the projected funding gap over the three-year period is between £11.5 million (based on an assumption of a 1% annual increase for AEF) or £14.5 million (based on an assumption of a zero increase in AEF) as shown in **Exhibit 3**.
- the Council has made a number of other assumptions in identifying the funding gap which have a direct impact on the estimations of the savings requirement each year. These include the effects of re-pricing the base budget, Council Tax base changes and the potential ongoing impact of Brexit, but exclude the possible financial impact of the COVID-19 pandemic from 2022-23 onwards.
- one of the main financial risks is a continuing overspend in Social Services.
- the Council has an extensive road network which needs maintaining and the Council is aware that this is an ongoing financial pressure.
- the Council has ambitious plans for regeneration and is setting aside money to achieve these.
- council tax collection rates were under pressure in early 2020-21 due to COVID-19, but these have improved towards the year-end and its active debt collection has contributed to this.

Exhibit 3: the Council has a total projected funding gap for the three years 2021-22 to 2023-24 of between £11.5 million and £14.5 million dependent on different assumptions of levels of AEF funding

This graph shows the funding gap that the Council has identified for the following three years.



The Council has continued its record of not making unplanned use of reserves to fund revenue expenditure, and usable reserves have increased in recent years

Why sustainable management of reserves is important

10 Healthy levels of useable reserves are an important safety net to support financial sustainability. As well as being available to fund unexpected funding pressures, useable reserves can also be an important funding source to support ‘invest to save’ initiatives designed to reduce the ongoing cost of providing services. Councils that show a pattern of unplanned use of reserves to plug gaps in their revenue budget that result in reductions of reserve balances reduce their resilience to fund unforeseen budget pressures in future years.

11 We found that:

- usable reserves have increased in recent years and the Council has continued its record of not making unplanned use of reserves to fund revenue expenditure. The Council has a Reserves Policy in place and has no plans to use general reserve balances to fund revenue budgets other than for exceptional and agreed priority one-off items.

- usable reserves have increased steadily during the period between 2016-17 and 2019-20 from £20.2 million to £27.7 million as shown in **Exhibit 4**.
- in 2019-20, usable reserve balances were 17.8% of the net cost services the Council delivers. This compares to the equivalent figures across Welsh councils of 33.4% being the highest and 4.2 % the lowest. (As shown in **Exhibit 5**.)
- with the exception of COVID-19 pressures, movements in the balance of reserves for 2020-21 are largely in line with those planned at the 2020-21 initial budget setting stage, with balances expected to rise to £28.2 million.
- funding of MTFP projects in 2021-22 is forecast to reduce planned usable reserves by £4 million (14%) to £24.2 million.
- earmarked reserves are intended to assist in funding the Council's long-term capital strategy and priorities in its economic and education plans.

Exhibit 4: amount of reserves versus annual budget

This exhibit shows the amount of usable reserves the Council had during 2019-20 and the previous three years as a proportion of the net cost of the services the Council delivers.

	2016-17	2017-18	2018-19	2019-20
Net Cost of Services in £ millions ²	£147.6m	£147.2m	£151.8m	£155.8m
Total Useable Reserves in £ millions ³	£20.2m	£21.5m	£24.2m	£27.7m
Total Useable Reserves as a percentage of net cost of services ⁴	13.7%	14.6%	15.9%	17.8%

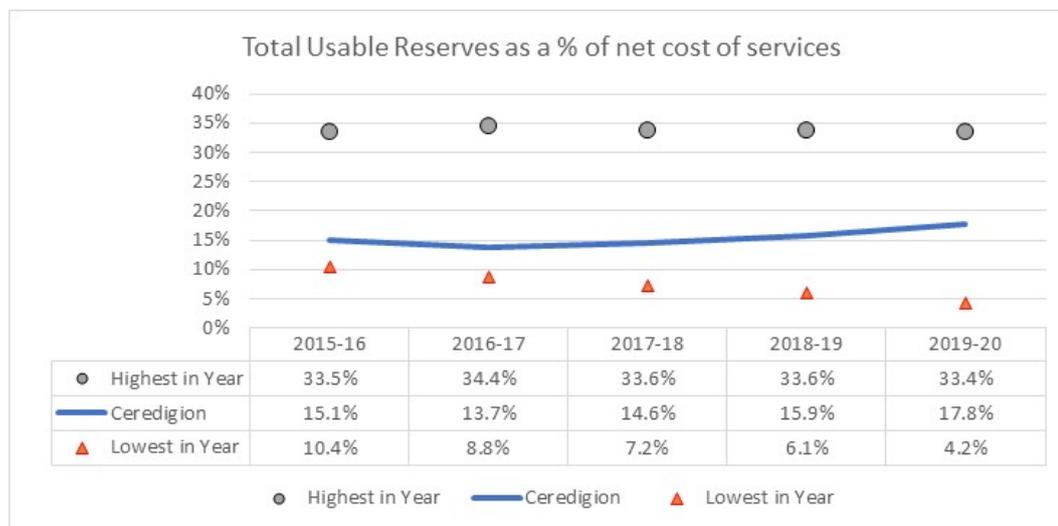
Source: audited statements of account 2016-17 to 2019-20

² Value used is the net cost of services charged to the general fund from the Expenditure Funding Analysis, less any Housing Revenue Account cost of services, plus precepts, levies and debt interest. Source: Statement of Accounts

³ By usable reserves we mean the total general fund balance, together with earmarked reserves that councils are not legally prevented from redirecting to use for another purpose. Source: Statement of Accounts

⁴ Audit Wales calculation.

Exhibit 5: comparison with all Welsh councils – Total Useable Reserves as a percentage of the net cost of services



The Council has a good track record of meeting its overall annual budget, although there continues to be significant overspends in Social Care

Why accurately forecasting expenditure is important

- 12 It is important that overspending and underspending are kept under control and that actual expenditure is as close to the levels planned as possible. A council that is unable to accurately forecast and plan expenditure runs the risk of creating unforeseen financial pressures that may compromise the ability to set a balanced budget. Significant patterns of underspending may be reducing the ability of a council to deliver its key objectives or meet its statutory responsibilities.
- 13 We found that:
 - robust financial management is serving the Council well and helping it to remain financially sustainable.
 - the Council has achieved small budget surpluses in recent years and is forecasting an overall year-end underspend of £0.3 million in 2020-21 as shown in **Exhibit 6**. This excludes direct COVID-19 financial elements which are managed on a corporate basis and reported separately.
 - as in previous years, there are continued and significant cost pressures within Social Care budgets. with an expected overspend in 2020-21 of £1.5 million.

- the Council has task and finish groups, spend review panels and budget performance challenge meetings to monitor the Social Services overspend.
- the transformation project within Social Services is ongoing.

Exhibit 6: amount of overspend/underspend relative to total net revenue budget

The following exhibit shows the amount of overspend or underspend for the Council's overall net revenue budget for the last four years and also the latest estimated outturn for 2020-21 as reported to the Council's Cabinet **16 March 2021**.

	2016-17	2017-18	2018-19	2019-20	2020-21
Original Net revenue budget £ millions	£132m	£135.2m	£140.2m	£143.6m	£151.2m
Actual Net Revenue Outturn	£131.9m	£134.7m	£140.2m	£143.6m	£150.9m
Amount of overall surplus/overspend	£0.1m	£0.5m	£0	£0	£0.3m
Percentage difference from net revenue budget	0.08%	0.4%	0%	0%	0.2%

Source – Budget setting and outturn reports to Cabinet and Council 2016-17 to 2019-20 and estimated outturn report to Cabinet for the year to date 2020-21

The Council has a good track record of meeting savings targets, however, delivering the required savings will be more challenging going forward

Why the ability to identify and deliver savings plans is important

- 14 The ability to identify areas where specific financial savings can be made, and to subsequently make those savings, is a key aspect of ensuring ongoing financial sustainability against a backdrop of increasing financial pressures. Where savings plans are not delivered, this can result in overspends that require the use of limited reserves whilst increasing the level of savings required in future years to compensate for this. Where savings plans are not delivered and service areas are required to make unplanned savings, this increases the risk either of savings not being aligned to the Council's priorities, or of 'short-term' solutions that are not sustainable over the medium term.
- 15 We found that:
 - the Council has a good track record of delivering a high percentage of its planned savings.
 - in 2018-19, the Council achieved 90% (£5.6 million) of its savings target and 90% (£5.4 million) of its target in 2019-20. (As shown in **Exhibit 7**.)

- for 2020-21, all of its planned savings of £0.7 million are expected to be fully achieved. Additional savings of £1.1 million, due to the impact of COVID-19 for reduced running costs, are also anticipated, although these are not currently considered a key part of its long-term savings plans.
- the Council's MTFP 2021-22 to 2023-24 has set two potential future savings targets over three years of either £11.5 million or £14.5 million subject to future AEF funding levels being confirmed.

Exhibit 7: savings delivered during 2019-20 as a percentage of planned savings

The following exhibit sets out how much money the Council intended to save from its savings plans during 2018-19 and 2019-20 and how much of this it actually saved, as well as estimated figures for 2020-21.

	2017-18	2018-19	2019-20	2020-21 estimate
Total planned savings in £ millions	£3.7m	£6.2m	£6m	£0.7m
Planned savings achieved in £ millions	£3.6m	£5.6m	£5.4m	£0.7m
Planned savings not achieved in £ millions	£0.1m	£0.6m	0.6m	£0m
Percentage of savings achieved	97%	90%	90%	100%

Source: budget setting and outturn reports to Cabinet and Council 2017-18 to 2019-20 and estimated outturn report to Cabinet and MTFP 2021-22 to 2023-24 for the year to date 2020-21

The Council has maintained favourable liquidity levels over recent years

Why the Council's liquidity position is important

- 16 Why gauging current assets to current liabilities (liquidity) is important:
- an indicator of how a council manages its short-term finances.
 - while it is commonly used to examine whether organisations are able to pay their debts in the short term, this is unlikely to be a risk for councils given their ability to take short-term borrowing. It does also, however, act as an indicator of how a council manages its short-term finances.
 - councils with low liquidity ratios should ensure they have arrangements in place to meet their liabilities.
 - there may be additional costs for councils that rely on short-term borrowing to pay debts.
 - councils with very high liquidity ratios should consider whether they are managing their current assets in the most effective way.
- 17 We found that:
- the Council has maintained favourable liquidity levels over recent years which are supporting its financial position.
 - as an indicator of the Council's liquidity position, we reviewed working capital ratios and found that these have remained relatively stable over the five-year period to 31 March 2020 ranging between 1.0 and 1.7 and averaging at 1.4 per annum. See **Exhibit 8**.

Exhibit 8: working capital ratio 2015-16 to 2019-20

	2015-16	2016-17	2017-18	2018-19	2019-20
Current Assets ⁵	£35.8m	£28.7m	£32.8m	£38.7m	£45.1m
Current Liabilities ⁶	£22.7m	£27.4m	£23.2m	£23.2m	£29.2m
Working Capital Ratio	1.6	1	1.4	1.7	1.5

Source: audited accounts 2015-16 to 2019-20

⁵ Current Assets includes: Short Term Investments; Assets held for sale; Inventories; Short Term Debtors; and Cash and equivalent.

⁶ Current Liabilities includes: Short Term Borrowing; Short Term Creditors; and Provisions due in one year.



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Council Response Form

Council action planned in response to the proposals for improvement issued by Audit Wales

Council: Ceredigion County Council

Report title: Financial Sustainability Assessment

Issue date: September 2021

No	Proposal for Improvement	Actions planned in response to proposal improvement issued by Audit Wales	Target date for completion of actions	Responsible Officer
P1	<p>To ensure the Council meets its future financial challenges, the Council should:</p> <ul style="list-style-type: none"> • continue to monitor the significant overspends in Social Care; and • ensure that the Social Services Transformation Project is driving improvement. 	<p>The Council accepts the Audit Wales proposal for improvement.</p> <p>Actions include:-</p> <ol style="list-style-type: none"> 1. Formal financial monitoring reports takes place with reporting to both Leadership Group and Cabinet; and 2. Action plans and work streams are being implemented and the Governance arrangements are in place to ensure that progress is made. 		

Financial Sustainability of Local Government

**COVID-19 Impact, Recovery
and Future Challenges**

September 2021

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Contents

Councils have received significant extra funding to deal with the pandemic, but the future sustainability of the sector remains challenging against a backdrop of other financial pressures.

Background – our work on local government financial sustainability over 2020-21	4
The bigger picture – borrowing, spending and demand pressures	5
Financial sustainability – key findings from our work	9
Four steps to help improve councils' financial sustainability	13
Audit Wales future work on councils' financial sustainability	15



Background

Our work on local government financial sustainability during 2020-21

Over 2020-21 we looked at the financial sustainability of each of the 22 councils in Wales, including:

- the financial impact of the pandemic;
- financial strategies;
- reserves position;
- performance against budget; and
- savings delivery and liquidity (the extent to which current assets are able to cover debt).

This report highlights some key themes and findings from our work, some commentary on funding pressures, and some reflections on how councils' future financial sustainability could be strengthened.



Main report

The bigger picture – borrowing, spending, and demand pressures

Extra short-term funding has helped but longer-term challenges and uncertainties remain

- The UK and Welsh Governments put in place major funding streams and grants in response to the pandemic – but these spending patterns are unlikely to be sustained.
- Our Picture of Public Services report published in September 2021 set out further information and analysis of public sector spending and future projections.
- Local government has a key role in supporting and shaping recovery from the pandemic, both as a provider of a wide range of key local services, and also through its community leadership role, including working with a range of partners.

Local government financial sustainability – how the situation in Wales compares with England

- England – the National Audit Office found that the financial position of local government remains a cause for concern with the outlook looking uncertain, and noted the reliance of many councils on using reserves to balance their 2020-21 budgets¹.
- Wales – councils have not generally relied on their reserves to balance their 2020-21 budgets, largely due to the additional funding made available to them to mitigate the impact of the pandemic. But significant future challenges remain.

1 National Audit Office, [Local government finance in the pandemic](#), March 2021

Exhibit 1: how councils’ usable financial reserves² had changed before the pandemic

All Wales total for unitary authorities, Total usable revenue reserves not protected by law

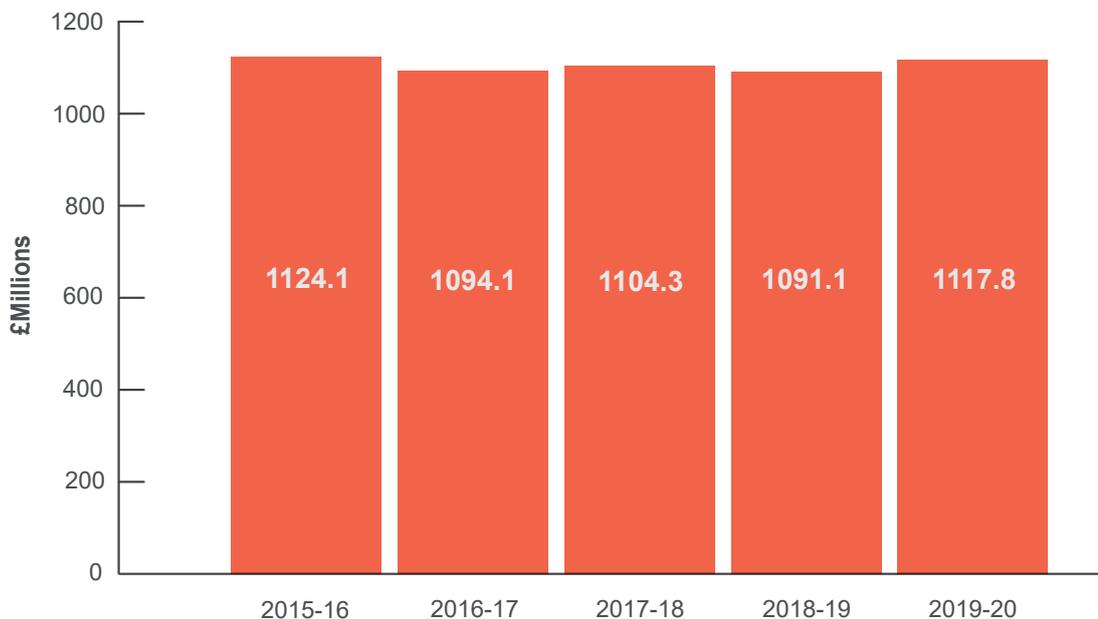
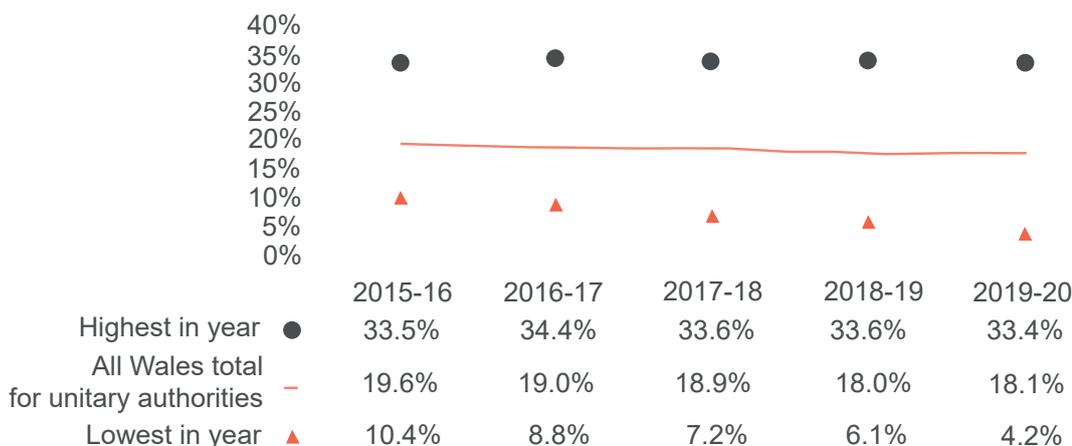


Exhibit 2: amount of usable reserves as a percentage of net cost of services over time

The following exhibit shows the average, highest and lowest values for the principal councils in Wales at the end of each financial year from 2015-16 to 2019-20.

Total Usable Reserves as a % of net cost of services



Lowest and highest refer to the value of an individual council in that particular year.

2 We define usable financial reserves as reserves usable for revenue costs, where the purpose is not protected by law. This is the total of the general fund, earmarked reserves and schools balances. It excludes Housing Revenue Account reserves, capital receipts and capital grants unapplied.

Public sector borrowing has increased during the pandemic and future funding levels are uncertain

- UK government borrowing has increased significantly during the pandemic³.
- Future funding levels remain uncertain, for example, in March 2021 Cardiff University described the outlook for the Welsh budget as ‘highly uncertain’⁴. The Chartered Institute of Public Finance & Accountancy (CIPFA) have also highlighted the uncertainty around public sector funding in the future.
- There is likely to be significant pressure on local government funding, in particular for those service areas that are not prioritised as part of future budget-setting⁵.

Demand for some services is likely to increase

- Our recent report on discretionary services⁶ highlights rising demand for some council services. The infographic on the following page, from that report, summarises some key demand pressures.
- Demand pressures from the pandemic will potentially continue, for example, for additional education provision to catch up on lost time during school closures. The longer-lasting implications of the pandemic on demand for local government services are as yet unknown.

Spending on discretionary local government services had already reduced before the pandemic

- Reductions in funding had already led to some service cuts before the pandemic⁷. Although the pandemic has raised the profile of local government services and in particular the role they play in helping to keep people safe and healthy.

3 CIPFA, [Local authorities face a financial reckoning](#), November 2020

4 Wales Fiscal Analysis, [Welsh Election 2021 Fiscal outlook and challenges for the next Welsh Government Welsh Election Briefing](#), April 2021

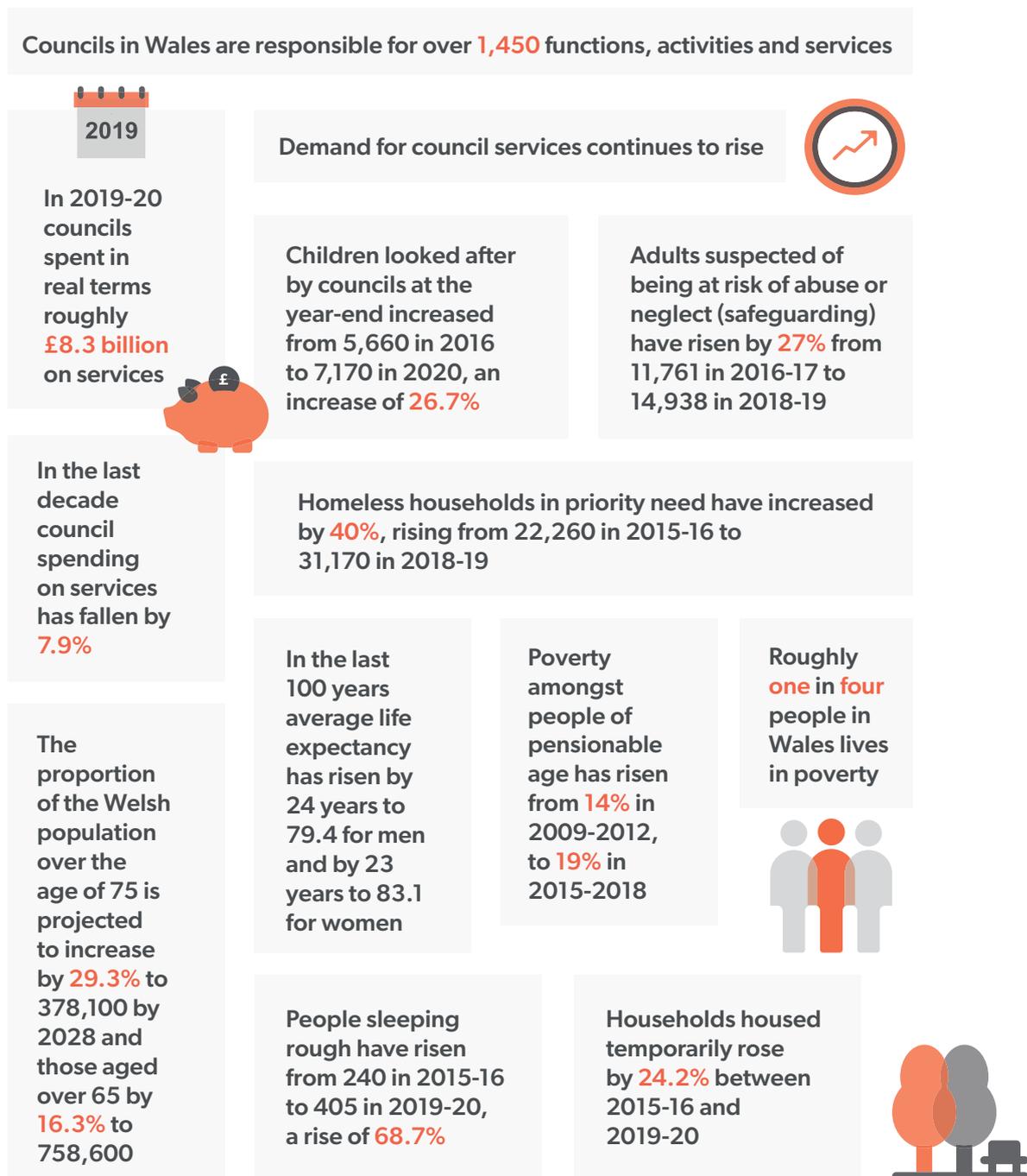
5 Wales Fiscal Analysis, [Local government finance: the state of play in 2021-22](#), March 2021

6 Audit Wales, [At your Discretion - Local Government Discretionary Services](#), April 2021

7 Audit Wales, [At your Discretion - Local Government Discretionary Services](#), April 2021

Exhibit 3: key facts about council services and demand⁸

The following exhibit shows some key facts about council services including some key demand pressures.



Note: The £8.3 billion figure for total council spending covers the total revenue spending on services and includes spending on some non-service areas such as repayment of borrowing, levies pensions and appropriations to reserves. The figure is net of income, such as charges and fees, generated by services. The gross expenditure on services in 2019-20 was £9.2 billion.

Financial sustainability – key findings from our work

Our findings from October 2020

- In October 2020, we said: ‘Councils and the Welsh Government have worked well together to mitigate the impact of the pandemic to date, but the future sustainability of the sector is an ongoing challenge.’ We also noted that ‘some Councils were better placed financially than others to deal with the financial challenges posed by the pandemic⁹.’

Overall findings from our work in 2020-21

- We found that Councils have received significant extra funding to deal with the pandemic, but the future sustainability of the local government sector remains challenging against a backdrop of other financial pressures.
- After publishing our national summary report in October 2020, we then looked at the financial sustainability of each principal council in Wales.
- We produced local reports for each council.
- Due to the extra funding councils have received in response to the pandemic, the financial position has improved for all 22 councils this year.
- But the overall picture of councils’ financial sustainability remains mixed, some councils are still better placed than others to respond to future challenges.
- The next section summaries the key themes we identified through this work, including where relevant from our October 2020 report as well as our previous work on financial sustainability.

9 [Audit Wales, Financial Sustainability of Local Government as a Result of the COVID-19 Pandemic, October 2020](#)

Key themes from our 2020-21 work

The financial impact of COVID-19

- We said in October 2020 that some councils were better placed financially than others to respond to the challenges of the pandemic.
- So far, the costs of COVID-19 have been mitigated at each council by extra funding from the Welsh Government.

Exhibit 4: The cost of COVID-19 over 2020-21

The following exhibit sets out the extra funding provided to councils by Welsh Government over 2020-21 in response to the COVID-19 pandemic.

- £660 million additional funding allocated by the Welsh Government to the Hardship Fund to cover councils' lost income and extra expenditure¹⁰.
- Other funding from the Welsh Government such as extra funding for teachers for catch-up support from education and cleaning materials for schools.
- Personal protective equipment (PPE) has also been provided free of charge to most local government bodies by the Welsh Government through NHS Shared Services.



Source: Welsh Government

Financial strategies

- Several councils have only undertaken limited analysis of the longer-term impact of COVID-19 (even in respect of working assumptions or scenarios) or the longer-term impact of changes to demand.
- Most, but not all councils include some council tax assumptions for the next four or five years in their financial strategies. These range from predicted increases of between 3% and 5%.
- Most, but not all, financial strategies also include Aggregate External Funding (AEF)¹¹ assumptions that vary between 0% and 3%. A few councils plan on the basis of best-to-worst-case scenarios.
- Overall, most of our local reports reflect on the ongoing work needed to develop a more sustainable approach to financial planning in the medium to long term.

¹⁰ Although the Welsh Government allocated £660 million, by the end of the financial year it reports having spent £587 million.

¹¹ Aggregate External Funding data includes Revenue Support Grant from the Welsh Government and Non-Domestic Rates.

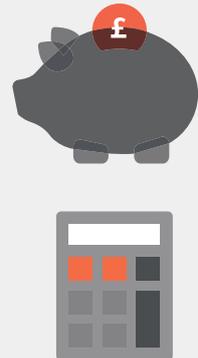
Reserves position

Exhibit 5: usable reserves – what we said in our October 2020 report¹²

The following exhibit summaries our key findings on councils' usable reserves¹³ position from our October 2020 report.

In October 2020 we reported:

- the usable reserves held by councils ranged from around £11 million to over £119 million.
- there was a wide range of usable reserves as a proportion of the net cost of services at each council: from 5% to 33%; and
- that Welsh councils in total held over £1 billion of usable reserves at the end of March 2020.



- Some councils have relatively high level of reserves that will support their ability to respond to challenges, and other councils have much lower levels of reserves, which will make meeting future challenges harder.
- After completing our local work we have also found that all councils increased the amount of reserves they held at the end of 2020-21. Councils have reported an increase of over £450 million in reserves during 2020-21. We will report further on this following our audit of 2020-21 accounts.
- Some councils have a good track record in recent years of avoiding using reserves to balance their budget.
- Some councils have relied on unplanned use of reserves to balance budgets. This approach is unlikely to be sustainable, particularly for those councils whose levels of usable reserves were already relatively low.
- A consistent pattern of using reserves, even in a planned way, to balance revenue expenditure is unlikely to be sustainable as it risks depleting reserves to unsustainable levels.

Performance against budget

- After large transfers to reserves, most councils reported either relatively small underspends or overspends overall in 2020-21, a similar pattern to the previous two financial years.

¹² Audit Wales, [Financial Sustainability of Local Government as a Result of the COVID-19 Pandemic, October 2020](#).

¹³ By usable reserves we mean the total general fund balance, together with earmarked reserves that councils are not legally prevented from redirecting to use for another purpose. This is the total of the general fund, earmarked reserves, and schools' balances. It excludes the HRA, Capital receipts and capital grants unapplied.

- Most councils also continued to show significant overspends in some service areas; in many councils, social services were an example of this.
- The pandemic, along with longer-term challenges, means that now more than ever, councils will need to manage budgets effectively and ensure that services or areas of consistent overspends are addressed.

Savings delivery

- Last year we found that most councils delivered the majority of their savings, but very few delivered all of their planned savings in previous years. We found the same pattern over 2020-21, as well as that some councils delivered all of their savings targets, although not as they had planned.
- Savings plans have understandably been affected by the pandemic. Changes in demand for services, workforce re-deployment and other action taken in response to the pandemic are all likely to have had an impact on the achievement of some savings.
- In a number of councils, service areas were still able to deliver their savings targets. Some service areas found it easier to deliver savings because of:
 - additional funding from the Welsh Government;
 - a reduced demand for services during the pandemic and/or;
 - reduced staff costs during the pandemic.
- Delivery of savings is likely to be even more challenging going forward given the scale of the projected funding gaps in some councils in future years, and that the above factors that helped some service areas to deliver savings over 2020-21 are unlikely to be recurring.
- Councils with robust and effective savings planning processes will be better placed to deliver on proposals and fulfil plans within the longer term.

Liquidity¹⁴

- Overall, most councils show a favourable and stable liquidity ratio (the ratio of current assets to its current liabilities) which suggests that those councils are in a good position to meet their current liabilities.
- A few councils show a relatively low liquidity ratio. In itself this is not a particular problem. But if levels of reserves are also relatively low and if savings are not being achieved, taken together this could indicate a lack of resilience.

¹⁴ Liquidity means the ratio of the council's assets to its liabilities

Four steps to help improve councils' financial sustainability

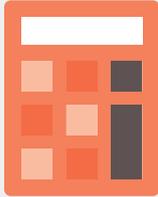
Exhibit 6: four steps to help with councils' financial sustainability

Based on the findings from our local work, together with the themes and challenges reflected on in this paper, the exhibit below summarises some key steps setting out what councils can do to improve financial sustainability.

1	<p>Financial strategies</p> 	<p>Understand short, medium and long-term challenges and clearly set out the overall priorities for the council's finances</p> <ul style="list-style-type: none"> • The Chartered Institute of Public Finance & Accountancy (CIPFA) highlights the uncertainty around public sector funding in the future, urging councils to use a range of data and forecasting work as part of their financial planning over the medium term¹⁵. • A clear and robust financial strategy is important to identify the likely level of funding available to a council, as well as the anticipated level of demand for, and cost of, providing services. • Given the anticipated funding pressures facing all councils, it is important to identify how to respond to those future pressures, and particularly how they will meet projected funding gaps. • Now is more important than ever to have a robust financial strategy that builds a picture of the council's financial situation over the medium to long term including well-evidenced projections around future demand pressures. • Councils should ensure that members are aware of, and understand, where their council's assumptions originate and where the assumptions sit in relation to those made by other councils. • The pandemic has also shown the benefits of building flexibility into financial strategies, and planning for different scenarios. Councillors should be presented with clear choices based on comprehensive and robust information including: <ul style="list-style-type: none"> - the total levels of reserves available to use; - future funding pressures; and - a full range of planning assumptions.
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2	<p>Reserves</p> 	<p>Plan your approach to, and use of, reserves to ensure that it supports longer-term financial sustainability</p> <ul style="list-style-type: none"> • Healthy levels of usable reserves are an important safety net to support financial sustainability. • As well as being available to meet unexpected funding pressures, usable reserves can also be an important funding source to support ‘invest to save’ initiatives designed to reduce the ongoing cost of providing services or for transformation programmes. • Regularly reviewing the levels of reserves and considering if levels are appropriate will help to set priorities around use of reserves. • Councils should ensure that councillors understand the role of both usable and unusable reserves, and how these link to the overall and longer-term financial strategy for the Council.
3	<p>Performance against budget</p> 	<p>Know what’s realistic for services to achieve and then understand and act on areas of consistent overspends</p> <ul style="list-style-type: none"> • It is important that overspending and underspending are kept under control and that actual expenditure is as close to the levels planned as possible. • A council that is unable to accurately forecast and plan expenditure runs the risk of creating unforeseen financial pressures that may compromise the ability to set a balanced budget. • Significant patterns of underspending may be reducing the ability of a council to deliver its key objectives or meet its statutory responsibilities. • Seek to manage budgets effectively throughout the year, as opposed to one-off budget exercises.

4

Savings delivery
Understand what is realistic for services to deliver on savings or cost reductions and act on areas that do not consistently deliver planned savings

- The ability to identify areas where specific financial savings can be made, and to subsequently make those savings, is a key aspect of ensuring ongoing financial sustainability.
- Where savings plans are not delivered this can result in overspends that require the use of reserves whilst increasing the level of savings required in future years to compensate.
- Where savings plans are not delivered and service areas are required to make unplanned savings, this increases the risk either of savings not being aligned to the Council's priorities, or of 'short-term' solutions that are not sustainable over the medium term.
- Now is more important than ever to get savings plans right, ensure that plans are realistic, and developed in collaboration between councillors, executive management teams and services.

Audit Wales future work on councils' financial sustainability

- For 2021-22, we will continue to monitor the financial position of individual councils through our ongoing audit work.
- Following completion of our audits of 2020-21 accounts we will also publish a financial sustainability data tool, including data on councils' year-end position for 2020-21, and continue to update this annually.
- We may undertake further work at some councils where we identify specific risks.
- We will return to national work in future where we believe the situation merits it and where we could add value.
- We will also consider the possibility of comparing the financial position of local government bodies in Wales with those across the UK as well as potential national work in relation to specific themes.
- In undertaking any potential future work, we will continue to engage with the Society of Welsh Treasurers.



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