Archwilio Cymru
Audit Wales

Financial Sustainability Assessment – Gwynedd Council

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Contents

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 March 2021.

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

Recommendations

Exhibit 1: proposals for improvement

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

Recommendations
Medium Term Financial Plan R1 The Council should update its Medium Term Financial Plan annually to support financial planning.
Budget Setting R2 The Council should further develop the use of activity data in setting its demand-led budgets.
Budget Review – Additional Grant Allocations and Transfers to Reserves R3 The Council should include significant grant allocations at service levels in its budget review and mitigate the effect of any in-year transfer to reserves to allow the transparent reporting of the financial position.
Review Savings Schemes R4 The Council should undertake at least annual reviews of historic savings schemes to ensure that they are still realisable.

The Council has a good understanding of its financial position, but several financial challenges remain

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

6 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.

7 We found that:

- the Council reacted quickly to the pandemic, reporting to Cabinet on 19 May 2020, **The Effects of COVID-19 on the 2020-21 budget**, identifying funding gaps and calling for Welsh Government support;
- the Council has incurred £14.6 million of additional COVID-19-related expenditure and £7.8 million loss of income during 2020-21, and receive £18.5 million from the Welsh Government Hardship Fund and £2.1 million from other Welsh Government Funding streams;
- an estimate £3.2 million additional expenditure and £0.2 million income loss that it will have incurred that has not been covered by additional funding;
- the 2020-21 budget assumes that the Welsh Government will continue to compensate additional costs and loss of income;
- the 2021-22 budget assumes that there is no change in demand nor reduction in income generating activities for most services because of the pandemic;
- the Council recognises that the pandemic made financial planning extremely challenging and identified a funding gap of up to £8 million for 2021-22 to the Cabinet on 13 October 2020 for financial planning purposes but did not publish a Medium Term Financial Plan;
- the report to Cabinet identified 12 factors amounting to an unprecedented level of financial uncertainty leading to the range of potential outcomes increasing widely beyond 2021-22 as the rationale for not producing a Medium Term Financial Plan; and
- the Council plans to publish its Medium Term Financial Plan for 2021-22 in the summer and has not calculated the impact of COVID-19 over the medium term.

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

The table below shows the Council's 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.

The additional amount the Council has spent as a result of COVID-19 over 2020-21.	£14.6 million
The amount of income the Council has lost as a result of COVID-19 over 2020-21.	£7.8 million
The amount of additional funding the Council will receive from the Welsh Government over 2020-21 to mitigate the impact of COVID-19.	£18.5 million
The cost to the Council of COVID-19 over 2020-21 after extra funding from the Welsh Government is taken into account.	£3.9 million
Additional funding from the Welsh Government to cover 'savings not achieved' and 'digital transformation'.	£2.1 million

The Council has a clear financial strategy for the current year but needs to plan more for the medium term and focus on improving sustainability

Why strategic financial planning is important

8 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 also important to identify how it intends to respond to those pressures, and particularly how they will meet projected funding gaps.

We found that:

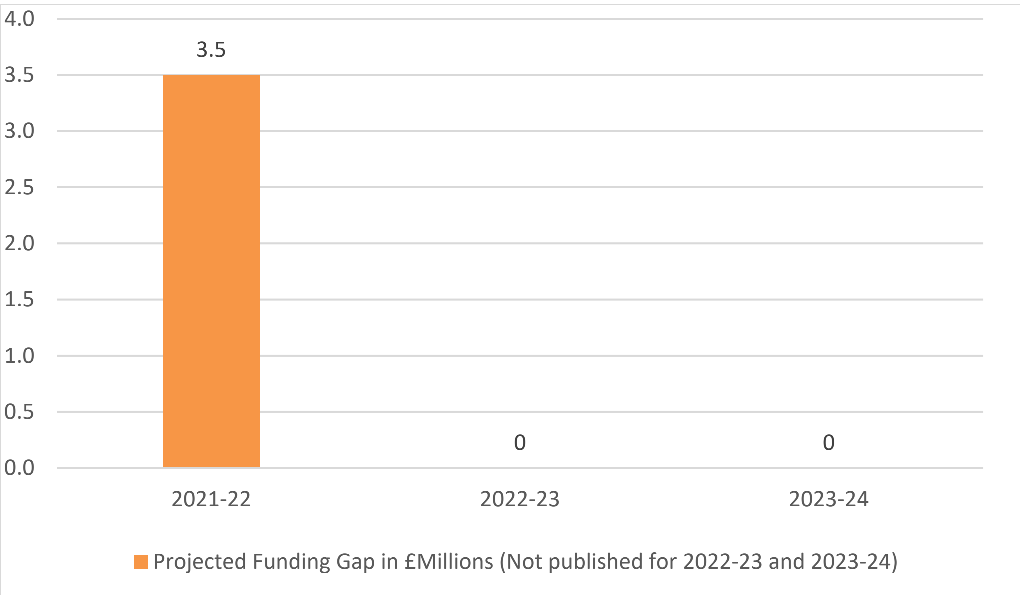
- we reported in our Gwynedd Council Financial Sustainability Assessment report published in March 2020 that **the Council is currently in a relatively strong financial position and its overarching financial strategy has supported financial resilience well; however, some services have**

significant annual overspends and not all savings are realised, posing a risk to financial sustainability in the longer term.

- the Council considers a multitude of financial and economic factors in setting its budget and uses demographic information to inform the levels at which key demand budgets are set.
- the Council has made significant additional budget allocations to key demand services as part of the budget setting process in recent years, but some services expenditure is still more than the available budget.
- whilst most of the Council's budgets are within budget at year-end, some of the key demand services, most notably Children and Supporting Families, have been under financial pressure for a prolonged period, raising concerns about the underlying assumptions used to underpin the budget setting process.
- the Council has plans, including potentially using its relatively high level of reserves to bridge its funding gap.
- the Council has delayed publishing the Medium Term Financial Strategy (for 2021-22 – 2023-24) until the summer of 2021, to await the UK Government Chancellor's Comprehensive Spending Review. The Council has not published a Medium Term Financial Plan to accompany the 2020-21 budget.
- the Council published its last Medium Term Financial Strategy on 7 March 2019, which considered the period 2019-20 to 2021-22.

Exhibit 3: the Council had a funding gap of £3.5 million in 2021-22 and has not published estimates for 2022-23 and 2023-24

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



The Council has a high level of reserves, most are controlled centrally and present an opportunity to transform and improve services

Why sustainable management of reserves is important

9 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.

We found that:

- the Council had £71.1 million of useable reserves at 31 March 2020, which is 26.4% of the net cost of services. Useable reserves increased to £99.6 million at 31 March 2021 which is 40.8% of the net cost of services[2].
- the Council's Usable Reserves have increased 86.5% over the last five years from 2017 to 2021.
- reserves are held in designated balances and a review of the names and descriptions of the earmarked reserves indicates that most balances are held centrally rather than by demand-led services.
- there appears to be little evidence to demonstrate the utilisation of reserves to improve and transform services, which may in turn support the financial sustainability of the Council.
- funding baseline commitments from one-off funding sources leads to unresolved funding pressure in future years' budget.

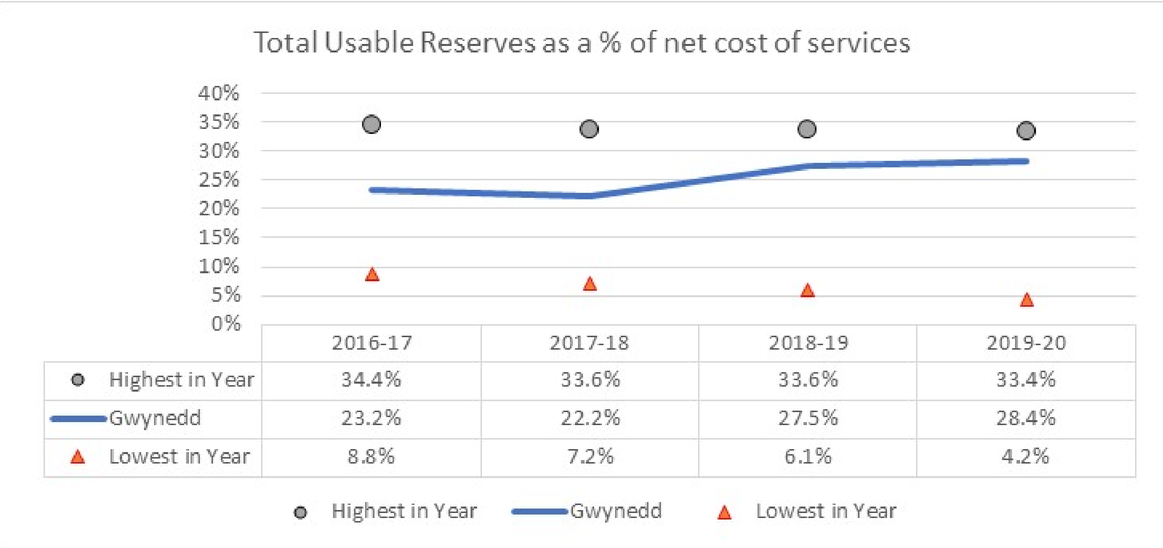
[2] Unaudited 2020/21 Statement of Accounts

Exhibit 4: amount of reserves versus annual budget

This exhibit shows the amount of usable reserves the Council had during 2020-21 and the previous four years as a proportion of the net cost of the services the Council delivers.

	2016-17	2017-18	2018-19	2019-20	2020-21
Net Cost of Services in £ millions [3]	230.0	235.9	235.7	250.1	244.2
Total Useable Reserves in £ millions [4]	53.4	52.4	64.9	71.1	99.6
Total Useable Reserves as a percentage of net cost of services [5]	23.2%	22.2%	27.5%	28.4%	40.8%
Comparison with the other councils of Wales	6/22	6/22	3/22	3/22	[2020-21 comparison not available]

Exhibit 5: Total Usable Reserves as a percentage of Net Cost of Services of principal councils in Wales 2019-20



[3] 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

[4] 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

[5] Audit Wales calculation.

The Council has recurring overspends in-year in key services, and budget monitoring reports vary from the final position reported at year-end

Why accurately forecasting expenditure is important

10 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.

What we found:

- the Council services before recommended adjustments overspent in 2019-20 and it was estimating an overspend at service level in 2020-21 in its 'End of November Review'.
- the 2020-21 'End of November 2020 Budget Review' does not accurately reflect the Council's financial position, as the estimated financial overspend of £4.69 million in the appendices does not include a transfer to reserves of £1.3 million and grant funding of at least £3 million. These two omissions collectively reduce the deficit of £4.69 million by £4.3 million to a significantly lower deficit of £390,000. Whilst the above was explained in the narrative report, the omission in the service analysis could mislead and confuse readers.
- the final 12-month figures for 2019-20 reported an outturn overspend of £2.6 million after estimating an overspend of £4.58 million in the 'End of November Review'.
- the Council's practice of transferring surpluses to reserves as part of its Budget management exercise effectively overstates the net estimated deficit at year-end. The transfer of £1.09 million of underspend to reserves in 2019-20 effectively increased the net overspend from £3.49 million to £4.583 million.
- the Council up to 2020-21 had identified but not addressed significant patterns of in-year overspending in some of its key services. Activity level information was not used to set budgets in key demand areas. Robust activity and cost data along with detailed analysis of trends over several years would enable the Council to set budgets based on actual service users rather than demographics. This would enable the Council to re-join the group of councils with services performing more consistently within budget.

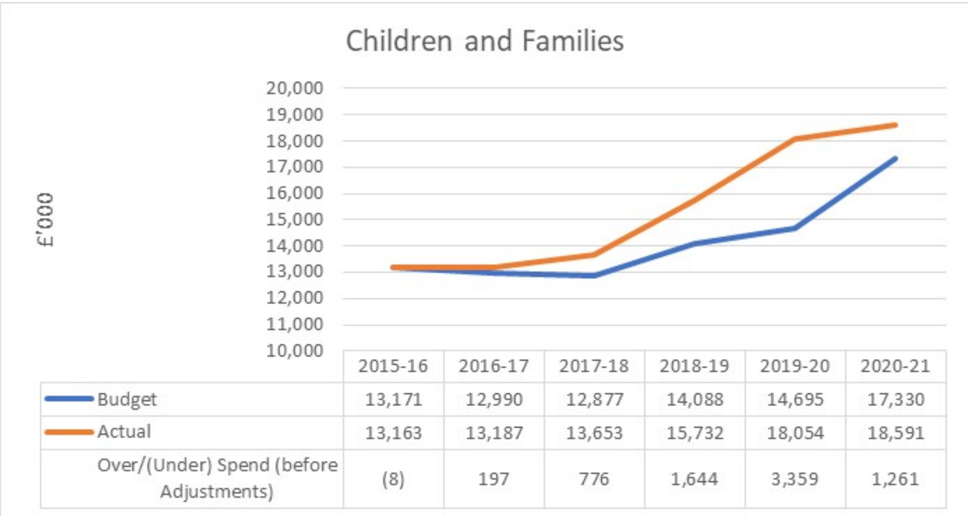
Exhibit 6: Amount of overspend/underspend relative to total net revenue budget

The following exhibit shows the amount of overspend or underspend for the Council's overall net revenue budget after transfers to and from reserves for the last four years. The Council does not report the proposed corporate budgets to cabinet as part of its Budgetary Reviews.

	2016-17	2017-18	2018-19	2019-20	2020-21
Original Net revenue budget £ millions [6]	241.0	246.0	259.6	265.4	280.3
Actual Net Revenue Outturn [7]	240.2	246.6	258.4	265.4	279.3
Amount of overall (surplus)/overspend [8]	(0.8)	0.6	(1.2)	0.0	(1.0)
Percentage difference from net revenue budget	-0.3%	0.2%	0.4%	0%	-0.4%

Exhibit 7: Performance against budget by service

The following exhibit shows the annual overspend in Children and Families Service. The Council has allocated additional budget to the service; however, actual expenditure still exceeds available budget.



[6] 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

[7] 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

[8] Audit Wales calculation.

Continued rolling forward of undelivered savings can create unresolved financial pressure for services; identifying and delivering savings will be more challenging going forward

Why the ability to identify and deliver savings plans is important

11 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.

What we found that

- during the period 2016-17 to 2019-20, the Council delivered on average 84% of savings schemes in the planned year of delivery.
- the Council continued to implement the undelivered element of savings plans, going on to deliver an average of 97% of planned schemes for the period 2016-17 to 2019-20.
- the Council recognises that the pandemic has had a significant impact on its delivery of savings, leading to £1.7 million of slippage into 2021-22, £1.0 million of schemes being reprofiled into 2022-23, and £0.8 million of schemes being deleted.
- recent performance suggests that it is more difficult to deliver all planned savings in the Social Care budgets within the year. The inability to deliver savings over a prolonged timespan suggests that planned savings may be unrealistic. Savings expectations not borne out of reality can lead to disillusion amongst those trying to meet unrealistic targets and budgets.
- as part of the review undertaken by Cabinet in January 2021, £1.4 million of savings schemes were deleted and £3.2 million were deferred into following years.

Exhibit 8: Savings delivered during 2016-17 to 2020-21 as a percentage of planned savings

The following exhibit sets out how much money the Council intended to save from its savings plans during 2016-17 to 2020-21 and how much of this it actually saved in the planned year of delivery.

	2016-17	2017-18	2018-19	2019-20	2020-21
Total planned savings in £ millions [9]	9.2	7.4	2.5	5.3	3.9
Planned savings achieved in £ millions in the planned year of delivery [10]	8.7	6.0	1.8	4.0	1.6
Planned savings not achieved in £ millions in the planned year of delivery	0.5	1.4	0.7	1.3	2.3
Percentage of savings achieved in the planned year of delivery	94.3%	80.9%	73.1%	75.6%	41.0%

12 The realisation of savings schemes within the Council's services is variable. Whilst some departments have delivered most or all the planned savings, there are 'Schemes slipping and with some risks to be achieved' over an extended period. This is particularly prevalent in Adults; Health and Well-being, Children and Supporting Families, and to a lesser extent in other services. The Council has deleted some of the savings, but a significant amount remains deferred for delivery in future years.

13 The Council continued to deliver savings that were not implemented in the planned year achieving an average of 97% during the period 2016-17 to 2019-20.

[9] 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

[10] 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

The Council's liquidity has been stable over the period 2015-16 to 2019-20 and has risen slightly in 2020-21

Why the Council's liquidity position is important

14 Why gauging current assets to current liabilities (liquidity) is important:

- it is 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.

15 We found that:

- the Council's liquidity has been broadly stable over the last five years and the relatively consistent liquidity presents no concerns about financial sustainability; and
- the Council does not anticipate any change to its liquidity position over the next three years.

Exhibit 9: working capital ratio 2015-16 to 2019-20

	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21
Current Assets [11]	98.6	83.8	105.6	91.4	104	150
Current Liabilities [12]	99.7	92.9	115	88.5	98.3	112
Working Capital Ratio	1.0	0.9	0.9	1.0	1.1	1.3

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

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

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