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Dear Will

Assurance and Risk Assessment Progress Update – Financial Position

Following on from our meetings earlier this year we said that we would more formally feedback on some specific aspects of our assurance and risk assessment work that we have undertaken. This letter provides a progress update on the Council's financial position.

This work was undertaken as part of our 2021-22 Assurance and Risk Assessment (ARA) project to help discharge the Auditor General's duties¹.

We recognise that the both the current and future financial climate is both challenging and fluid and therefore this feedback provides a point in time assurance and risk progress update on the Council's financial position for 2021-22.

¹ These duties include under section 17 of the Public Audit (Wales) Act 2004 (the 2004 Act). It may also inform a study for improving value for money under section 41 of the 2004 Act, and/or an examination undertaken by the Auditor General under section 15 of the Well-being of Future Generations (Wales) Act 2015.

Financial Position update 2021-22

What we did

We undertook our assessment of the Council's 2021-22 Financial Position between September and November 2022. The evidence was gathered through interviews and document reviews and included consideration of the Council's financial reserves position, the delivery of planned savings and performance against the planned budget for the year. Whilst the focus of our work was on the 2021-22 financial year, where appropriate, consideration has also been given to later financial information where this helps to contextualise the position.

We also published a [Local Government Financial Sustainability Data Tool](#) in February 2022 which includes a range of financial data for councils, national parks and fire and rescue authorities in Wales.

What we found

The Council has retained a stable financial position, including through achieving planned savings and additional Welsh Government funding, to maintain balanced budgets and has increased its useable reserves. But the Council will need to develop a sustainable financial plan to address the substantial emerging cost pressures.

Financial strategy

The draft Medium Term Financial Plan (MTFP) for 2022-23 to 2025-26 for Pembrokeshire County Council was approved by Council in March 2022. This plan outlined the financial strategy for the Council going forward, including options for Council Tax increases, the allocation of additional funding to services, and potential savings opportunities.

The March 2022 MTFP noted that the Council had made £81.3 million of cost reductions and efficiencies in the previous eight financial years.

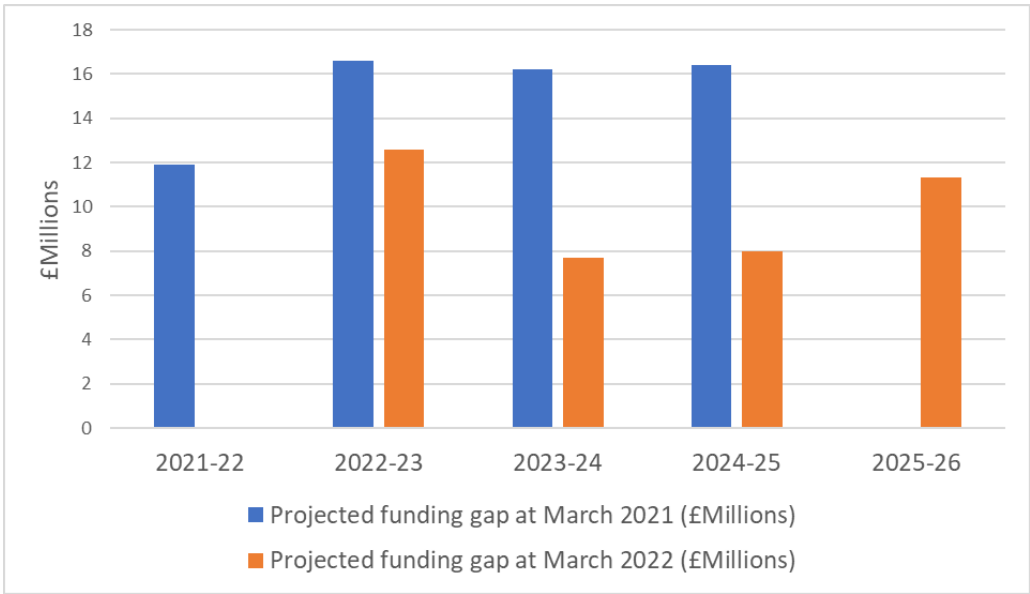
The March 2022 MTFP also updated the Council's projected funding gap. The gap for the 2022-23 financial year is projected to be £12.6 million, a decrease of £4 million compared to the figure projected in the MTFP published in March 2021.

The March 2022 MTFP projects funding gaps for 2023-24 and 2024-25 to be smaller than previously thought. They are now projected to be £7.7 million and £8.0 million

respectively, compared to the projected figures in the March 2021 MTFP of £16.2 million and £16.4 million respectively.

The decrease in the projected funding gap outlined in the March 2022 MTFP is due to the cumulative impact of a projected improved Aggregate External Finance (AEF) of +9.4% in 2022-23, 3.5% in 2023-24 and +2.4% in 2024-25.

Exhibit 1: the funding gap in 2022-23 is now larger than previously projected, but will decrease in 2023-24 and 2024-25 compared to previous projections

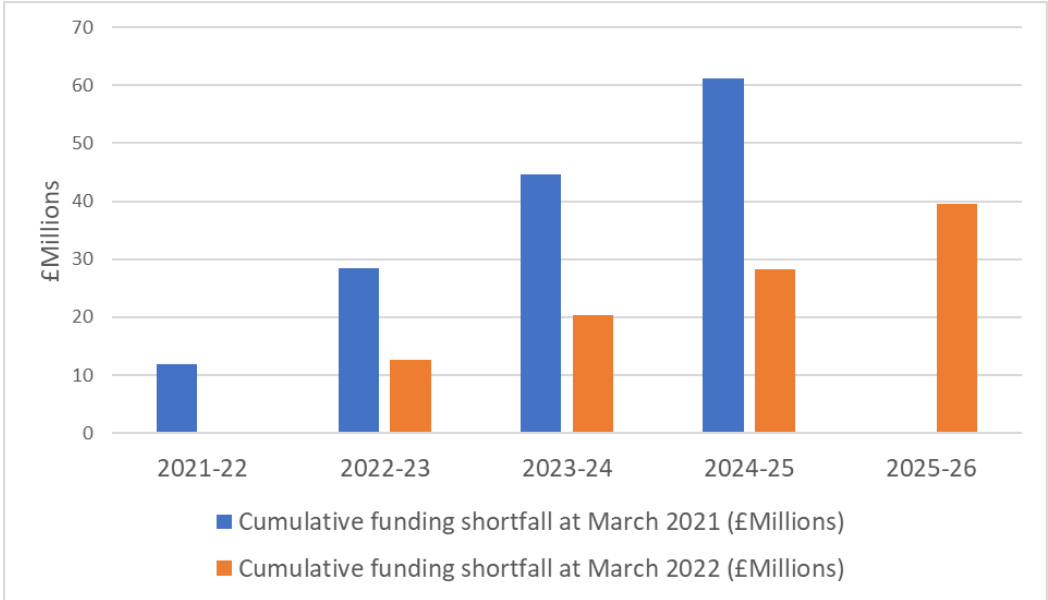


The March 2022 MTFP also updates the projected cumulative funding gap facing the Council up to 2025-26. Whilst the projected gap is more than halved by 2024-25 compared to the figure in the March 2021 MTFP, it is still a considerable sum at £28.3 million.

The March 2022 MTFP states that this gap will be filled primarily from increased Council Tax income and identified budget savings with services.

The Council's projected budgeting includes a Council Tax increase of 5% per year. The March 2022 MTFP does note that despite increases in the four financial years up to 2021-22, the Council still has the lowest Band D Council Tax in Wales. At £1,189, this rate is £172 lower than Carmarthenshire and £223 lower than Ceredigion.

Exhibit 2: the March 2022 MTFP projects the Council’s cumulative funding gap to be reduced from the figures published in the March 2021 MTFP



Useable reserves

Over the last four financial years, up to the end of 2021-22, the Council’s useable reserves have increased from £46.43 million to £83.023 million, a difference of £36.59 million.

Although the net cost of services has also risen over the same four year period, the useable reserves were 24.5% of the net cost of services in 2021-22. This percentage has increased in the last three financial years.

In 2020-21, the Council had the tenth-highest percentage of useable reserves compared to net cost of services.

The Council’s policy for the use of reserves changed in the March 2022 MTFP. Because of the ‘significant projected funding gap for 2022-23’, the Council may use reserves to balance its budget or fund the cost of workforce reductions if appropriate. The Council states that this use will be seen as a ‘one-off’, accompanied by a clear plan to reduce base budgets from 2023-24 onwards and replenish the reserves balance over the full course of the March 2022 MTFP.

Exhibit 3: useable reserves have increased in the last four years, but this has been accompanied by a similar increase in the net cost of services.

	2017-18	2018-19	2019-20	2020-21 ²	2021-22 ³
Net Cost of Services (£Millions)	221.73	232.76	242.09	255.4	242.3
Total Usable Reserves (£Millions)	43.13	46.44	45.75	62.64	83.02
Total Usable Reserves as a percentage of net cost of services (%)	19.5	20.0	18.9	24.5	34.3
Comparison with the other councils of Wales	10th	9th	10th	11th	n/a

Savings delivery

In August 2021, Audit Wales published a Financial Sustainability Assessment of the Council, which included reporting on the Council's previous record on savings delivery. We noted that in the previous two financial years (2019-20 and 2020-21) the Council achieved 66% and 47.5% of its planned savings respectively. This record meant that £5.3 million and £4.2 million of savings were not achieved, placing further pressures on future budget rounds.

In the 2021-22 financial year, the Council planned to save £7.506 million. At the year end, they had achieved £6.088 million, 81.1% of the original target. This is an improved performance compared 2019-20 and 2020-21.

² Figures up to 2020-21 sourced from Audit Wales Financial Sustainability tool

³ Figures for 2021-22 sourced from unaudited statement of accounts published in December 2022

Performance against budget

The Director of Resources updated on the outturn monitoring for 2021-22 to Cabinet in July 2022. At the end of the financial year, net expenditure was £242.3 million. This was made up from gross expenditure of £399.5 million, income of £178.1 million and an end of year contribution to reserves of £20.9 million.

These figures showed lower expenditure than projected and higher income. The lower expenditure was mainly due to a reduction in capital financing costs, and the higher income was a result of the receipt of unplanned-for grants, including the Welsh Government Hardship Fund.

Future pressures

The Welsh Government's indicative funding settlements on an all-Wales basis of 3.5% and 2.4% respectively for 2023-24 and 2024-25 provide a degree of funding certainty over the medium term. However, medium-term financial planning will continue to rely on a range of assumptions, and when coupled with the changing socio-economic landscape in this period of significant economic uncertainty, planning for financial resilience and future budget rounds will continue to be challenging for councils.

The March 2022 MTFP outlined the substantial funding gap projected over the next four financial years. The Council planned to fill this gap with savings and service efficiencies, an increase in Council Tax, and a proposed one-off use of reserves in 2022-23.

The Council states that the use of reserves is not an ongoing solution to bridging its funding gap. The March 2022 MTFP also outlines the degree of savings already made in the previous eight financial years, and that this provides a difficult backdrop against which to propose more savings. The Council states that Council Tax rates are low in Pembrokeshire, any that increases would place an additional burden on residents.

It should also be noted that since the MTFP was published in March 2022, additional financial pressures have emerged that will affect both the Council and its residents.

The Chief Executive has told Audit Wales that the Council's projected deficit for 2023-24 is now in the region of £26 million to £32 million.

The cost of electricity, gas and fuel has risen steeply. The rate of inflation has also risen, and the cost-of-living crisis is also impacting on household budgets.

A Financial Resilience Strategic Business Risk paper was presented to the Corporate Overview and Scrutiny Committee on 18 October 2022. This provided an update on the Council's financial position going forward, based on the changes in circumstances since the publication of the March 2022 MTFP.

This paper states that the projected funding gap for the next three financial years will 'increase significantly', and that the financial climate is likely to get worse.

This paper also states that 'work is ongoing' to re-calculate the funding gap for 2023-24, but the Council estimates that this is now £24.4 million, compared to the figure of £7.7 million published in the March 2022 MTFP.

Medium-term financial planning will continue to rely on a range of assumptions, and when coupled with the challenging socio-economic landscape in this period of significant economic uncertainty, planning for financial resilience and future budget rounds will continue to be challenging for councils.

Yours sincerely,

Audit Wales