Archwilio Cymru
Audit Wales

Financial Sustainability Assessment – Wrexham County Borough 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 January 2021 to March 2021.

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

Recommendations

Exhibit 1: recommendations

The table below sets out the recommendations that we have identified following this review.

Recommendations
Reserves R1 Review the Council's level of reserves in the context of potential risks and ensure they are maintained at a level that supports its ongoing financial sustainability.
Managing spend R2 Ensure better alignment of budgets and operational activity to maintain ongoing financial sustainability.
Savings R3 Review how effectively planned savings were delivered in 2020-21 and ensure that robust arrangements are in place to identify, plan and deliver future savings.

The Council’s ongoing financial sustainability will only be assured if service pressures are more effectively managed

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 has claimed from the COVID Hardship fund to cover the financial impact of the pandemic.

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.

The additional amount the Council estimates it will have spent as a result of COVID-19 over 2020-21.	£13.6 million
The amount of income the Council estimates it will have lost as a result of COVID-19 over 2020-21.	£4.7 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.	£18.3 million
The cost to the Council of COVID-19 over 2020-21 after extra funding from the Welsh Government is taken into account.	£0.2 million
Additional fixed and hypothecated funding from Welsh Government to cover ‘savings not achieved’ and ‘digital transformation’.	£2.2 million

The Council has an MTFP covering the period 2021-2024; some assumptions require further refinement and the Council does regularly update it as information becomes available

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.

9 Public services have been significantly impacted by the pandemic and, in this context, mitigating the impact on councils will not only depend on the actions that they are able to take, but also to a large degree on the amount of resources allocated by governments. We recognise that a key issue for councils in trying to financially plan over the medium term remains uncertainty around both the level of funding they will receive from government, and their own income streams, such as council tax and fees and charges.

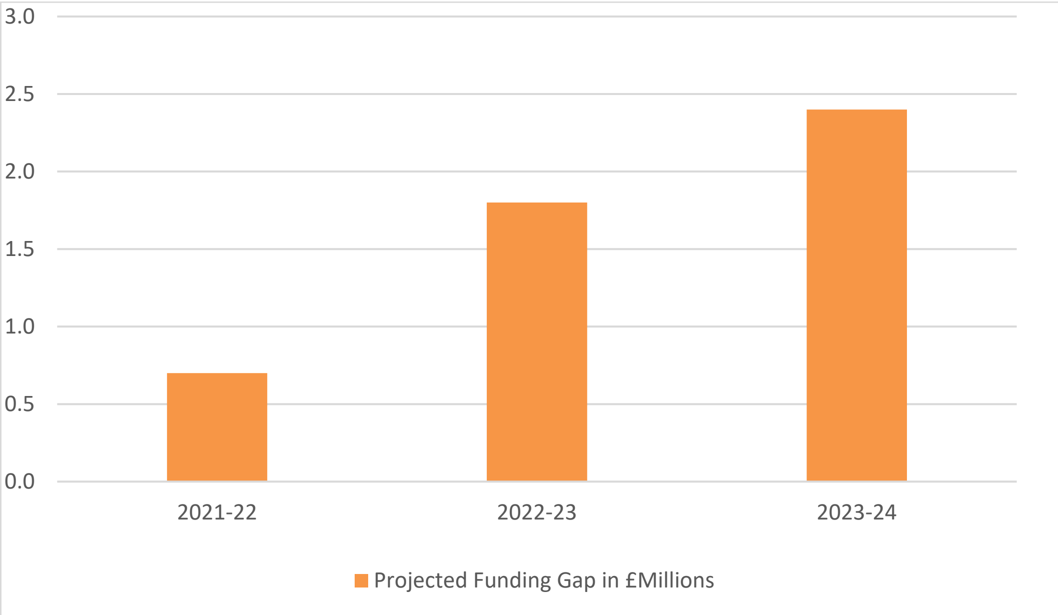
10 We found that:

- our 2019-20 Financial Sustainability report found that the Council's Medium Term Financial Plan (MTFP) did not set out how it would meet the projected cumulative deficit of almost £10 million between 2020-21 and 2021-22.
- the Council has now extended its financial planning to cover the period 2021-22 to 2023-24 which highlights a funding gap of £4.2 million over the years 2022-23 and 2023-24. **Exhibit 3** shows the breakdown of the gap over the lifetime of the MTFP.
- the Council's MTFP 2021-22 to 2023-24 identified the following risks that could result in the need to use reserves:
  - economic conditions, that are likely to result in real-terms reductions in revenue support grant and specific grants;
  - reduced capital receipts and planning-related income;
  - increased demand on services resulting in departmental overspends;
  - lower-than-expected income;
  - uninsured losses from hard-to-predict events;
  - uninsured legal liabilities;
  - inability to deliver planned savings;
  - costs as a result of organisational restructuring;
  - long-term contract costs; and
  - repair or replacement of assets.

- the Council's MTFP provides a good description of internal and external financial pressures such as funding issues, population forecasts, the Council's reserves strategy and its capital strategy. In the financial summary, it assumes increases in funding of 2% in Revenue Support Grant and 5% from Council Tax. It also recognises unavoidable commitments for demography, capital financing, Fire Service levy, free school meals, Council Tax Reduction Scheme (CTRS), Members' allowances and non-teachers pensions totalling £3.2 million over 2022-2024. Increased take-up of free school meals and CTRS represents changes in service demand; the provision for increased funding to cover demographic changes is not explained within the MTFP (due to the Council not having access to the relevant data at that time). Other increases are mostly formula based. As such, the MTFP provides a basic forecast of the Council's finances up to 2024 with provision of £0.5 million for 'demography' and a £4.2 million funding gap suggesting the MTFP requires further refinement.

Exhibit 3: the Council has a total projected funding gap for the three years 2021-22 to 2023-24 of £4.2 million

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



Source: MTFP 2021-22 to 2023-24

The Council could be vulnerable if reserves reduce to compensate for unexpected pressures

Why sustainable management of reserves is important

11 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.

12 We found that:

- our 2019-20 Financial Sustainability report found that the Council had not made any unplanned use of reserves to fund revenue budget pressures and its level of useable reserves had increased in recent years.
- **Exhibit 4** below shows the Council's total useable reserves as a percentage of the net cost of services have remained at around 12%, although in 2019-20 this fell to 11.6%. This percentage of useable reserves was the sixth lowest compared to all Wales councils.
- the graph in **Exhibit 5** shows that the Council's useable reserves as a percentage of its overall revenue budget are reducing year on year and that its percentage is much lower than some other councils.
- with earmarked reserves of over £20 million, the Council is well placed to fund many of the risks identified above. However, earlier in 2020-21, the Council forecast an overspend for looked-after children of £8 million; if this had materialised and not been offset by underspends in other services and additional Welsh Government funding, it had the potential to reduce reserves significantly.
- the revenue budget 2021-22 does not propose drawing on reserves.

13 Whilst the Council held useable reserves of £26.2 million as at 31st March 2020, in practice some of these should only be used for specific purposes. Within the Council's earmarked reserves were schools' balances of £2 million, a capital reserve of £2.2 million, an insurance reserve of £2.7 million and a financial instruments reserve of £3.1 million.

Exhibit 4: amount of reserves versus annual budget

This exhibit shows the amount of useable 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
Net Cost of Services in £ millions [2]	240.8	239.9	249.9	255.8
Total Useable Reserves in £ millions [3]	24.9	25.9	28.9	26.2
Total Useable Reserves as a percentage of the net cost of services [4]	10.3%	10.8%	11.6%	10.2%
Comparison with the other councils of Wales	18th	18th	14th	16th

Source: Statement of Accounts

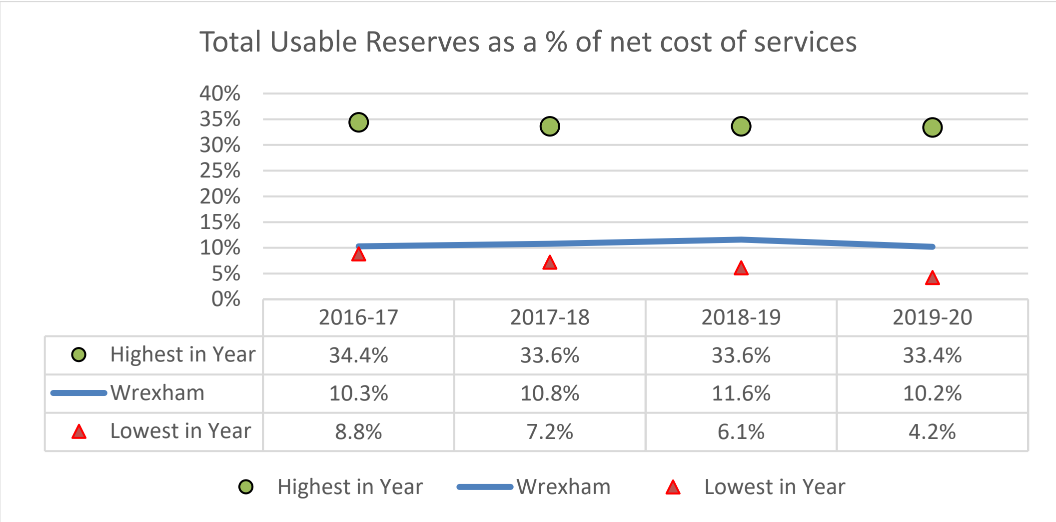
[2] Value used is the net cost of services charged to the general fund from the Expenditure Funding Analysis, less any Housing Revenue Account cost of services, plus precepts, levies and debt interest.

[3] By useable 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: amount of reserves versus annual budget

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



Source Financial Statements

The Council has a track record of balancing its revenue budget, but this has sometimes been as a result of additional income or a technical adjustment

Why accurately forecasting expenditure is important

14 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.

15 What we found

- our 2019-20 Financial Sustainability report found that the Council manages spending within its overall budget, but in recent years significant overspends in some services had been offset by large underspends in others and one-off windfalls. **Exhibit 7** shows further analysis of the budget variations.

- in 2018-19 we saw sizeable variations, although the Council underspent its revenue budget overall by approximately £0.2 million. Significant overspends in Environment and Planning of £0.9 million and Social Care of £0.7 million were offset by underspends in Finance of £0.3 million, Corporate and Central Services of £1.5 million, Finance and Investment of £0.3 million and Schools of £0.2 million. Full details are included in **Exhibit 7**.
- in 2019-20, the Council reported a net underspend of £0.3 million. Within this figure, Environmental and Technical Services overspent by £0.7 million, Children's Services overspent by £0.9 million and Planning and Regulatory Services overspent by £0.2 million. These overspends were offset by various service underspends, including an underspend of £1.4 million in Central Services and £0.3 million in Schools. Full details are included in **Exhibit 7**.
- in 2020-21, the Council reported a net underspend of £9.9 million. Within this figure, Social Care overspent by £5.6 million, (the Children's Services overspend of £6.8 million was offset by an underspend in Adult Services of £1.3 million). Other more notable underspends included schools – £7.5 million, Central Services – £3 million and Environment and Technical – £2.3 million. Full details are included in **Exhibit 7**.
- in recent years, the Council has benefited from additional income and accounting adjustments that have offset service overspends. These include a technical accounting adjustment and Welsh Government funding, including some COVID Hardship payments.
- these overspends and underspends indicate some misalignment between operational activity and the service budgets, and the Council is holding contingency funds centrally to cover in-year variances.

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 year to date as at January 2021.

	2016-17	2017-18	2018-19	2019-20
Original Net revenue budget £ millions [5]	224.0	225.3	232.9	236.9
Actual Net Revenue Outturn [6]	223.5	224.0	232.6	236.6
Amount of overall surplus/overspend [7]	0.5	1.3	0.3	0.3
Percentage difference from the net revenue budget	0.2%	0.6%	0.1%	0.1%

Source – Revenue Outturn reports 2018-19, 2019-20 and All Member Budget Briefing January 2021.

Exhibit 7: performance against budget by service

Service	2018-19	2019-20	2020-21
Environment and Technical		£661k over	£2,278k under
Planning and Regulatory		£185k over	£328k under
Environment and Planning	£877k over		
Housing and Economy	£2k under	£41k over	£472k under
Social Care	£748k over	£900k over	£5,557k over
Education and Early Intervention		£107k under	£812k under
Education	£128k over		
Finance and ICT		£133k under	£334k under
Finance	£278k under		
Governance and Customer Services		£88k under	£202k under
Corporate and customer services	£88k under		
Chief Executive		£181k under	£204k under

[5] 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

[6] By useable 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

[7] Audit Wales calculation.

Service	2018-19	2019-20	2020-21
Repairs and Maintenance	£2k under	£4k under	
Central Services	£1,477k under	£1,376k under	£3,061k under
Financing and Investment Income and Expenditure	£265k under	£92k over	£248k under
Schools	£191k over	£292k under	£7,542k under
Total net over/underspends	**£168k under**	**£302k under**	**£9924k under**

The Council has a track record of identifying and delivering savings although not always as planned

Why the ability to identify and deliver savings plans is important

16 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.

17 What we found:

- our 2019-20 Financial Sustainability report found that the Council has a good track record of identifying and delivering financial savings.
- in 2020-21, the Council identified savings amounting to £1.6 million. The All Member Budget Briefing in January 2021 reported progress in achieving the savings. The £0.5 million social care saving was described as 'Off track due to COVID' and savings in ICT, community centre housing and legal services were only partly achieved. All other savings were either achieved as planned, losses of income were covered by COVID hardship grants and other savings targets were replaced by other savings such as vacancy management.
- where savings have not been achieved, the Council considers these to have been covered by departmental underspending.
- the use of underspends to offset savings targets is a short-term fix and indicates that Council decisions have not been implemented. A further £690,000 of savings are to be found in 2021-22; managers will therefore need to understand why savings have not been achieved as planned, whether they can be delivered in future years and the impact of unplanned underspends on delivery of Council priorities.

The Council has maintained a liquidity ratio of below 1 over the period from 2016-17 to 2019-20 as planned

Why the Council's liquidity position is important

18 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.

19 We found that:

- the Council has had a liquidity ratio of below one since 2016-17. The Council has used short-term borrowing in line with advice from its Treasury Management Advisors to help maintain a lower cost of debt financing.
- the Council's liquidity ratio has been below the average across all Welsh Councils over the five-year period 2015-16 to 2019-20 (see **Exhibit 8**), but has a Treasury management strategy in place to meet its liabilities.
- the strategy is reviewed annually and is subject to scrutiny by members of the Governance and Audit Committee.

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

	2015-16	2016-17	2017-18	2018-19	2019-20
Current Assets [8]	38.6	33.0	44.2	53.8	57.8
Current Liabilities [9]	29.8	44.4	89.8	79.7	83.8
Working Capital Ratio	1.3	0.7	0.5	0.7	0.7

Source – data collection tool completed by the Council

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

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

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