Financial Sustainability Assessment – Carmarthenshire County Council

Audit year: 2020-21

Month/Year issued: September 2021

Document reference:

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 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 June 2021.

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

The Council is well placed to maintain its financial sustainability and has plans in place to deliver the efficiency savings needed to meet its identified future funding gap

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:

- Overall, the majority of the Council's COVID related expenditure and lost income was covered by Welsh Government and UK funding.
- The Council has estimated that approximately £0.7m of additional expenditure/income loss during 2020/21 will not have been covered by the additional funding received from Welsh Government.
- The full year effect of COVID is forecasted as additional expenditure of £22million and lost income of £10 million.
- The Medium-Term Financial Plan (MTFP) has incorporated a £500k contingency for social care and £1m contingency in response to COVID-19.
- Many critical services have continued throughout the pandemic, and in some areas expanded to meet excess demand.
- An economic stimulus package of £3.7m to support local business in response to the COVID-19 pandemic has been identified as a priority within the capital programme in 21/22. The priorities of this stimulus package relate to specific areas for boosting economy of Carmarthenshire and these include capital infrastructure, Town centre regeneration and digital infrastructure.

Exhibit 1: the cost to the Council of COVID-19 over 2020-21 [Carmarthenshire County Council]

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.	£22 million
The amount of income the Council estimates it will have lost as a result of COVID-19 over 2020-21.	£9.9 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.	£31.2 million
The cost to the Council of COVID-19 over 2020-21 after extra funding from the Welsh Government is taken into account.	£0.7 million

The Council's strategy has helped it to maintain a strong financial position to date

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:

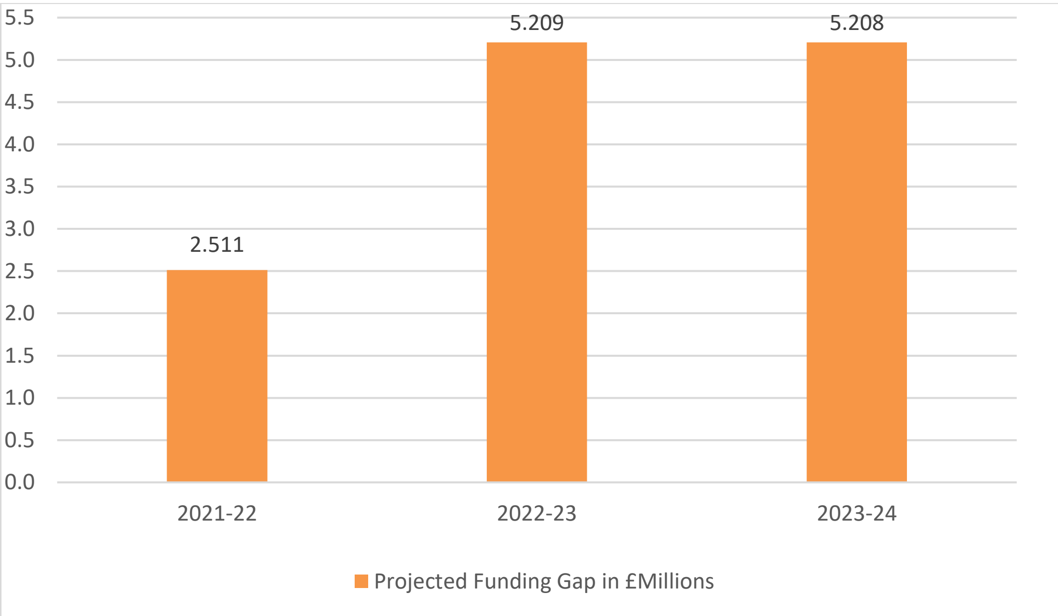
- In 2019-20 we reported that the Council's budget strategy was to allow for funding of necessary pressures/forecast changes in demand to develop a 'budget gap' which is then addressed through a mix of efficiencies, service reductions/closures, income generation or increases in council tax.

- In 2020-21 this approach has remained unchanged and has continued to allow the Council to maintain a strong financial position. In March 2021 the Welsh Government announced a 3.8% increase to the Council's revenue support grant for 2021-22. The Council has updated its Medium-Term Financial Plan to take account of this improved settlement.

- The Council has identified a funding gap of £12.9 million up until 2023-24. This gap assumes an annual increase in Welsh Government Funding of 2% per annum for 2022-23 and 2023/24. This funding gap has reduced from previous predictions due to the increased settlements received from Welsh Government in 2019-20 and 2020-21.
- The most significant cost uncertainty for the Council relates to future pay costs for all council staff. The previous assumption for the MTFP was an annual increase of 2.75%. This assumption has now reduced to 2.50% in the revised MTFP which has helped reduce the identified funding gap.

Exhibit 2: the Council has a total projected funding gap for the three years 2021-22 to 2023-24 of £12.9 million [Revenue Budget Strategy 2021/22 – 2023/24]

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



The Council continues to retain a high level of useable reserves, but it plans to reduce these significantly to fund its capital programme in future years

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

10 In 2019-20 we reported that the Council has a high level of useable reserves that have increased in recent years, but it plans to reduce these significantly over the next two years to fund its capital programme.

11 We reached this conclusion because:

- The Council had £93.9.m of useable reserves including a General Fund Reserve of £10.4m as at 31st March 2019.
- School Balances amounted to £3.7m as at 31st March 2016. Between 1st April 2016 and 31st March 2019 this has reduced to a deficit position of £400k because of the need to fund unplanned overspends on the delegated schools' budget. A further deterioration of £3m was expected in this reserve by 31st March 2020.

12 As at 31st March 2021, the Council had £134.1m of useable reserves including a General Fund reserve of £12.0m. Between 1st April 2017 and 31st March 2021 useable reserves have increased by 69.2%.

13 The Council plans to use a £46m of its earmarked reserves to help fund its capital programme between 2021/22 – 2023/24 and it is predicting that by 31st March 2023 earmarked reserves will have reduced to £29.3m. However, the Council plans to revisit its predictions due to its increased reserves position as 31 March 2021.

14 The Council has continued not to make unplanned use of reserves to fund revenue expenditure

Exhibit 3: amount of reserves vs annual budget (Annual statement of Accounts)

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 [2]	350,929	355,171	371,374	373,888	371,527
Total Useable Reserves in £ millions [3]	85,147	92,438	93,898	100,837	134,105
Total Useable Reserves as a % of net cost of services [4]	24.3%	26%	25.3%	27.0	36.1%

In 2020-21, the Council has delivered an underspend position against its overall net revenue budget but has seen some overspends in demand led services which was addressed through the use of departmental reserves

Why accurately forecasting expenditure is important

15 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

16 In 2019-20 we reported that in recent years the Council has reported relatively small overspends against its overall net revenue budget, with overspends in some departments and schools but this has been addressed in part through use of departmental reserves

[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.

17 For 2020-21, the Council reported a year end underspend of £0.814m against the net revenue budget for the year.

18 Our 2019-20 report made reference to pressures and budget overspends in the education department and some other demand led services. For 2020-21, the Education department underspent by £883k, the Communities department overspent by £393k, the Chief Executive's department underspent by £267k, the Corporate Services department underspent by £433k and the Environment department underspent by £243k. The main areas within the Communities department overspending related to physical and learning disabilities and mental health services.

Exhibit 4: amount of overspend/underspend relative to total net revenue budget (Budget Monitoring reports)

The following exhibit shows the amount of overspend or underspend for the Council's overall net revenue budget for the last four years.

	2017-18	2018-19	2019-20	2020-21
Original Net revenue budget £ millions	334.2	345.8	351.3	371.6
Actual Net Revenue Outturn	333.5	345.2	355.0	370.8
Amount of overall surplus/overspend	0.7m	0.6m	(3.7m)	0.8m
Percentage difference from net revenue budget	0.2%	0.08%	1%	0.22%

The Council performance in delivering planned savings has deteriorated in 2019-20 and 2020-21 and further work is needed to identify the required savings for the next three years

Why the ability to identify and deliver savings plans is important

19 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

20 In 2019-20 we found that the Council delivered most of its planned savings for 2017-18 and 2018-19 but was projecting to deliver less of its planned savings for 2019-20. We reached this conclusion because:

- In 2017-18 the Council delivered £5.6m of savings against a target of £6.9m.
- In 2018-19 the Council delivered £7.392m of savings against a target of £8.046m.
- The Council predicted that it would achieve £5.8m of savings against a target of £8.9m.

21 The Council achieved £5.7m savings against a target of £9m in 2019/20. Of the undelivered savings £2.1m were from the schools delegated budget. For 2020-21, due to the impact of Covid 19, the Council achieved £2.6m of their £5.1m of planned savings.

22 For the period 2021/22 to 2023/24, the Council has identified that it needs to deliver savings amounting to £10.96m. As at March 2021, the Council has identified specific savings totalling £9.1m for this period. The shortfall of savings required of £1.9m will need to be found over the next 12 months and the Council is working to identify these additional savings.

Exhibit 6: savings delivered during the period 2017-18 to 2020-21 as a percentage of planned savings

The following exhibit sets how much money the Council intended to save from its savings plans during the period 2017-18 to 2020-21 and how much of this it actually saved.

	2017-18	2018-19	2019-20	2020-21
Total planned savings in £ millions	6.9m	8.0m	9.0m	5.1m
Planned savings achieved in £ millions	5.6m	7.4m	5.7m	2.6m
Planned savings not achieved in £ millions	1.3m	0.6m	3.3m	2.5m
Percentage of savings achieved	81.2%	92.5%	63%	51.0%

The Council's liquidity position is sound, enabling it to meet its financial obligations when they fall due

Why the Council's liquidity position is important

23 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.

We found that:

- The working capital ratio for Carmarthenshire has remained stable over the previous 5 years ranging between 1.2- 1.6. A liquidity ratio of between 1 and 3 is considered healthy and indicates that the Council is in good financial health. This means that current assets have been well above the value of current liabilities and indicates that the Council can meet its financial obligations when they fall due without the need for short term borrowing.
- The Council adopts a prudent approach to treasury management, prioritising low risk before investment return and only investing surplus monies when adequate liquidity is maintained.
- The Councils liquidity ratio has exceeded the average across all Welsh Councils over the previous four years since 2016/17 indicating that it is in a comparatively strong financial position.

Exhibit 7: working capital ratio 2015-16 to 2019-20 (Source: Annual Statement of Accounts)

	2016-17	2017-18	2018-19	2019-20	2020-21
Current Assets [5]	89.9	95.5	105.6	123.2	167.7
Current Liabilities [6]	72.7	71.9	67.5	87.4	102.5
Working Capital Ratio	1.2	1.3	1.6	1.4	1.6

[5] Current Assets, includes: Short Term Investments; Inventories; Short Term Debtors; and Cash and equivalent

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

Audit Wales
24 Cathedral Road
Cardiff CF11 9LJ

Tel: 029 2032 0500
Fax: 029 2032 0600
Textphone: 029 2032 0660

E-mail: info@audit.wales
Website: www.audit.wales

We welcome correspondence and telephone calls in Welsh and English.
Rydym yn croesawu gohebiaeth a galwadau ffôn yn Gymraeg a Saesneg.