

Financial Sustainability Assessment – Neath Port Talbot Council

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Contents

The Council is well placed to maintain its financial sustainability and plans to strengthen some aspects of its financial management.

What we looked at and why 4

The Council is well placed to maintain its financial sustainability and plans to strengthen some aspects of financial management 5

The immediate impact of COVID-19 on the Council's financial sustainability has been mitigated by additional Welsh Government funding 5

The Council is working towards developing a sustainable medium-term financial strategy 6

The Council has a healthy level of useable reserves 7

The Council has a good track record of delivering services within agreed budgets 9

The Council has a track record of achieving most of its planned savings 11

The Council's liquidity position is sound, enabling it to meet its financial obligations when they fall due 12

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 2020-21 as at January 2021. 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.

The Council is well placed to maintain its financial sustainability and plans to strengthen some aspects of financial management

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 incurred significant extra expenditure and lost income in 2020-21 as a result of the COVID pandemic. The majority of this has been reimbursed by the Welsh Government and has not therefore had a detrimental effect on the Council's financial position. The Welsh Government has announced additional COVID-related grant funding for the first six months of 2021-22, but the extent of any further financial support and the longer-term effects of the pandemic on the Council's financial position are uncertain.
 - the Council identified and made provision for a number of the impacts of the COVID pandemic when setting its 2021-22 revenue budget and also included a £2.1 million contingency provision for general cost pressures and pay and pensions.
 - subsequent to agreeing the 2021-22 revenue budget, the Welsh Government provided further COVID-related grant funding at the end of March 2021, and the Council transferred £2.5 million to its earmarked corporate contingency reserve for future years' corporate priorities including COVID recovery costs.

Exhibit 1: 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 spent as a result of COVID-19 over 2020-21.	£14.5 million
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The amount of income the Council lost as a result of COVID-19 over 2020-21.	£9.5 million
The amount of additional funding the Council will receive from the Welsh Government over 2020-21 to mitigate the impact of COVID-19.	£23.6 million
The cost to the Council of COVID-19 over 2020-21 after extra funding from the Welsh Government is taken into account.	£0.47 million

Source: Council's finance department

The Council is working towards developing a sustainable medium-term financial strategy

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:

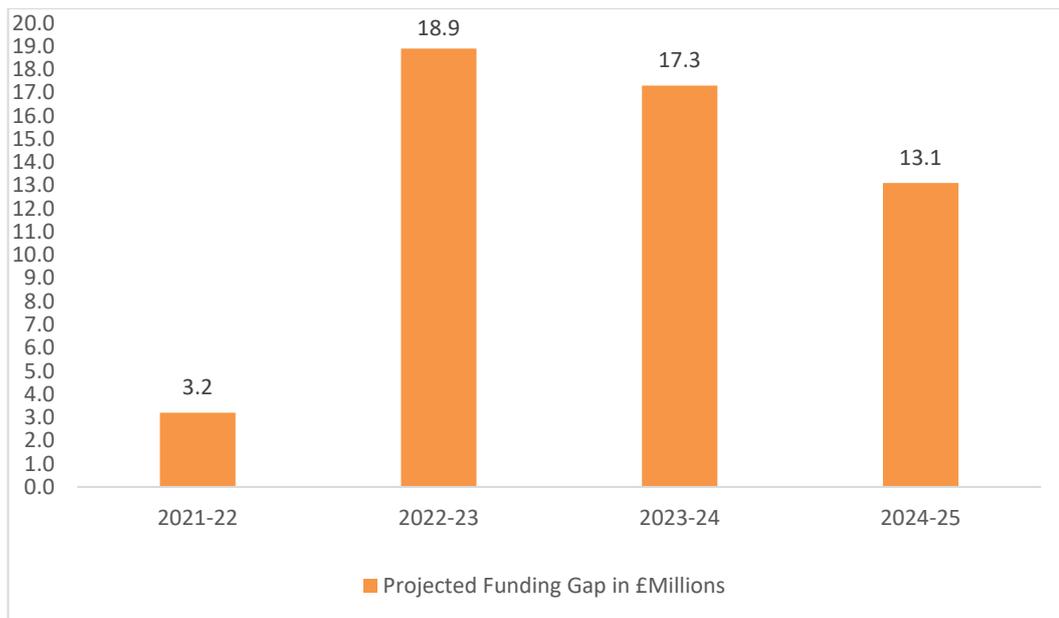
- in 2019-20, we reported that the Council focusses primarily on annual budgeting, did not have a published Medium Term Financial Plan (MTFP) and had scope to strengthen its medium-term financial planning and its links to the achievement of its corporate objectives.
- the Council revises its financial plan annually to help inform the annual budget setting process. The plan sets out the Council's medium-term financial projections and for the three-year period 2022-23 to 2024-25, the Council is projecting a funding gap of £49 million (in addition to the £3.1 million gap funded from general reserves in 2021-22).
- the Council has not made any changes to its approach to developing its medium-term financial projections, as it has prioritised its response to the COVID pandemic. Its projections continue to be based on prudent assumptions for inflation and known cost pressures but only reflect some assumptions in respect of demographic changes and service demand pressures. The Council plans to undertake further work to develop the forward financial plan and identify sustainable efficiency savings with a view

to producing an MTFP linked to the Council's corporate objectives by autumn 2021.

- as the Welsh Government does not provide any indicative funding assessment of future years, the Council's projections do not assume any funding growth in future settlements. In prior years, the Council has received more generous settlements than anticipated (4.5% in 2020-21, 4.2% in 2021-22) and if settlements continue to increase in future years, the financial gap will reduce by an estimated £2.3 million for every 1% variation in the settlement.

Exhibit 2: the Council has a total projected funding gap for the four years 2021-22 to 2024-25 of £52.4 million

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



Source: 2021-22 budget report to Cabinet

The Council has a healthy level of useable reserves

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.

10 We found that:

- in 2019-20, we reported that the Council had a healthy level of useable reserves and did not have a history of using reserves to fund revenue budget pressures.
- in setting its 2020-21 budget, the Council planned to use £1.65 million of its general reserves to balance its revenue budget. The Council forecast (at 8 March 2021) that its net revenue budget will underspend and, after receipt of COVID-related grants from the Welsh Government, projects that the general reserve will increase by £1.96 million. Since the forecast outturn position was reported to Members, the Council has received additional COVID-related grant funding from the Welsh Government which will increase its useable reserve balance further.
- the Council's budget for 2021-22 has been balanced with the use of £3.1 million of general reserves and at the time the budget was set, usable reserves were projected to be £53.6 million at 31 March 2022. The Council considers that the general reserve, which is projected to be 5.3% of its net revenue budget, will remain at a reasonable level and does not plan any further use of its general reserve to fund its medium-term financial deficit.
- whilst this use of reserves in 2012-22 will reduce the overall level of reserves available to the Council, these are still projected to remain at a reasonable level.

Exhibit 3: the net cost of services versus the amount of usable reserves

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 Estimate
Net Cost of Services in £ millions ²	283.3	281.8	296.1	307.0	N/A
Total Useable Reserves in £ millions ³	51.3	59.5	61.4	59.1	58.1

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

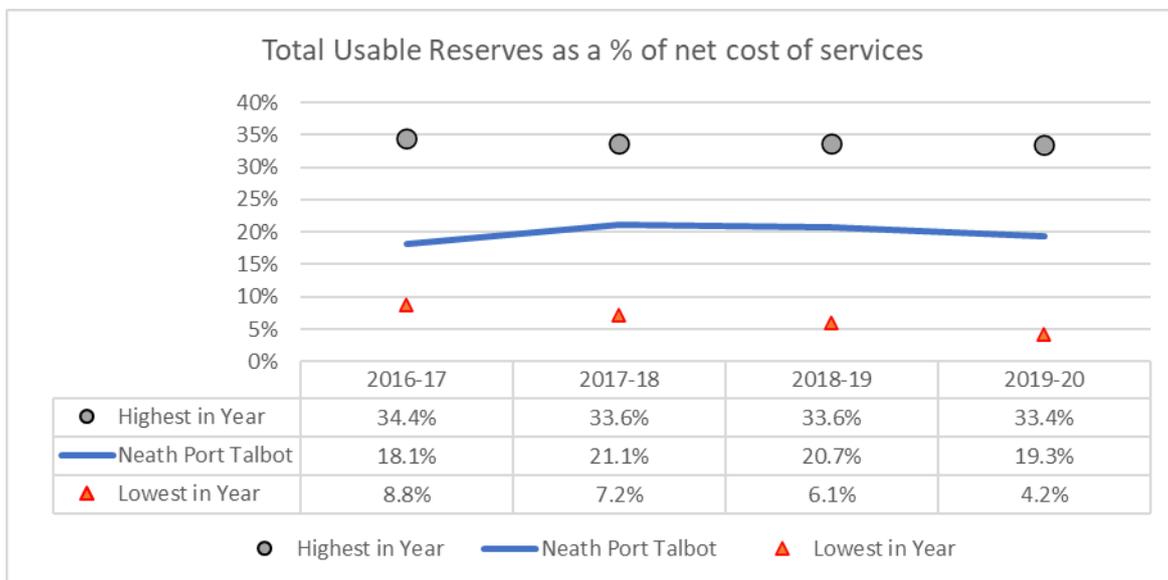
³ By usable reserves, we mean the total general fund balance, together with earmarked reserves that councils are not legally prevented from redirecting to use for another purpose. Source: Statement of Accounts

	2016-17	2017-18	2018-19	2019-20	2020-21 Estimate
Total Useable Reserves as a percentage of the net cost of services ⁴	18.1%	21.1%	20.7%	19.3%	N/A

Source: Annual statements of accounts

Exhibit 4: total useable reserves as a percentage of the net cost of services

The Council has maintained a level of usable reserves between 18.1% and 19.3% over the period 2016-17 to 2019-20.



Source: Audit Wales analysis

The Council has a good track record of delivering services within agreed budgets

Why accurately forecasting expenditure is important

- 11 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.

⁴ Audit Wales calculation.

What we found

- 12 In 2019-20, we reported that the Council had a good track record of financial management and had consistently delivered its services within agreed budgets, although overspends in some areas were offset by underspends elsewhere.
- 13 The Council underspent its revenue budget each year in the period 2016-17 to 2019-20 and transferred small surpluses to its reserves. For 2020-21, the month 10 revenue budget monitoring report projected a £1 million underspend. However, since this report was prepared, additional COVID-related grant monies have been received from the Welsh Government, which have further improved the outturn position.
- 14 Our 2019-20 report referred to pressures and budget overspends in education (home to school transport, out of county placements), some areas of children's social services and environmental services (refuse collection). The budget monitoring report to Cabinet in March 2021 reported that for 2020-21, education was projected to overspend by £90,000, social services to underspend by £1.15 million and environment to overspend by £994,000. The main causes of these variances are COVID related and due to additional Welsh Government funding; the underlying position is unclear in some areas.

Exhibit 5: 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 8 March 2021.

	2016-17	2017-18	2018-19	2019-20	2020-21
Original Net revenue budget £ millions ⁵	270.90	274.68	282.86	288.17	304.08
Actual Net Revenue Outturn £ millions ⁶	268.90	273.60	282.85	287.01	303.08
Amount of overall surplus/overspend £ millions ⁷	2.00	1.08	0.01	1.16	1.00
Percentage difference from net revenue budget	0.7%	0.4%	0%	0.4%	0.3%

Source: revenue outturn reports to Cabinet, revenue budget monitoring report as at 31 January 2021 presented to Cabinet 8 March 2021

⁵ Value used is the net cost of services charged to the general fund, plus precepts, levies and debt interest. Source: Council's budget reports to Cabinet

⁶ Value used is the net cost of services charged to the general fund, plus precepts, levies and debt interest. Source: Council's outturn reports to Cabinet

⁷ Audit Wales calculation.

The Council has a track record of achieving most of its planned savings

Why the ability to identify and deliver savings plans is important

- 15 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

- 16 In 2019-20, we reported that the Council had made significant savings in recent years and achieved the majority of its planned savings. Although the Council had a track record of balancing its budgets, it had not delivered all the specific savings it planned and budget underspends had been used to meet the shortfall.
- 17 The Council has made savings of £29.09 million between 2016-17 and 2019-20 (**Exhibit 6**). In 2019-20, the Council balanced its budget through planned savings of £5.8 million to address its budgeted funding gap. In 2020-21, this target was set at £1.97 million.
- 18 The achievement of savings is not separately monitored – individual agreed savings are removed from budgets at the start of the year and are monitored through the budget monitoring process. It is assumed that most of the in-year savings are delivered unless highlighted as a significant variance in the quarterly budget monitoring report to Members. The outturn position for 2019-20 and projected position for 2020-21 confirm that the Council has achieved most of its planned savings.
- 19 In common with other councils, identifying and delivering savings are becoming more challenging. Responding to the COVID pandemic has reduced the Council's opportunities to identify service changes and, for 2021-22, a savings target of only £135,000 has been set. The Council plans to balance its budget by using £3.1 million of general reserves.
- 20 The Council recognises that the use of reserves to balance its budget is not sustainable and further work to update the MTFP to 2024-25 will focus on identifying efficiencies to meet the projected £49 million funding shortfall over the next three years, which is in addition to the £3.1 million gap funded from general reserves in 2021-22.

Exhibit 6: savings delivered as a percentage of planned savings

The following exhibit sets how much money the Council intended to save from its savings plans between 2016-17 and 2019-20 and how much of this it actually saved as well as estimated figures for 2020-21.

	2016-17	2017-18	2018-19	2019-20	2020-21 estimate
Total planned savings in £ millions	11.55	5.78	6.79	5.80	1.97
Planned savings achieved in £ millions	10.72	5.78	5.06	5.33	1.97
Planned savings not achieved in £ millions	0.83	0.00	1.73	0.47	0.00
Percentage of savings achieved	93%	100%	75%	92%	100%

Source: budget reports and annual outturn reports to Cabinet

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

- 21 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.
- 22 We found that:
- the Council's liquidity position has been relatively stable over the period 2015-16 to 2018-19, increasing to 1.9 in 2019-20. This means that current assets were almost double 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 level of short-term investments increased significantly by 31 March 2021, which will lead to a further increase in the liquidity ratio to an estimated 2.3. The Council forecasts that the level of short-term investments and its estimated liquidity ratio will reduce to historic levels in 2021-22.
- the Council's liquidity ratio has historically exceeded the average for Welsh councils, which indicates that it is in a comparatively strong financial position.

Exhibit 7: liquidity (working capital) ratio 2015-16 to 2019-20

	2015-16	2016-17	2017-18	2018-19	2019-20
Current Assets £ millions ⁸	114.7	110.9	110.9	95.2	107.4
Current Liabilities £ millions ⁹	72.2	75.3	73.4	61.5	57.4
Liquidity Ratio	1.6	1.5	1.5	1.5	1.9

Source: Annual statements of accounts

⁸ Current Assets: includes Short Term Investments; Assets held for sale; Inventories; Short Term Debtors; and Cash and equivalent. Source: Statement of Accounts

⁹ Current Liabilities: includes Short Term Borrowing; Short Term Creditors; and Provisions due in one year. Source: Statement of Accounts



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