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## Financial Challenges Facing Local Government

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Dear June,

1. Following our correspondence in July 2014 and your appearance before the Committee on the financial challenges facing local government, the Public Accounts Committee has continued to consider this issue, taking into account recent related studies by the Auditor General, as well as evidence sessions held by the Committee. I am writing to set out some of the Committee's findings, and in particular where we believe the Welsh Government could provide more support to local authorities in overcoming the financial challenges they face.
2. The particular Auditor General reports the Committee has considered since our last correspondence have included *Delivering with Less – the Impact on Environmental Health Services and Citizens* (October 2014), *Managing Early Departures Across Public Bodies in Wales* (February 2015) and *The Financial Resilience of Councils in Wales* (April 2015). The Committee has held evidence sessions with representatives of Rhondda Cynon Taf, Gwynedd, the Vale of Glamorgan and Powys county councils.
3. This has been considered separately to the Auditor General's report *Managing the Impact of Welfare Reform Changes on Social Housing Tenants in Wales*, which the Committee will discuss with you on 2 June.



## Financial Challenges

4. The Committee heard clearly that the financial challenges faced by local government had moved beyond finding efficiencies in the delivery of public services, to changing the way services are delivered or discontinuing them altogether. In your 14 May 2015 response to the Auditor General's report on Financial Resilience of Councils in Wales, you noted that you did not recognise a figure the report presented as the scale of funding reductions faced by local government. It would be helpful to understand what the Welsh Government's assessment of that figure would be and how the Welsh Government and local government engage to ensure a shared understanding of the challenges faced by local government.
5. Your letter also set out that the Welsh Government provides additional support to local authorities where evidence suggests there is a need. It would be helpful to understand more about this additional support, including which local authorities had received additional support and the nature of this support.
6. A key issue that the Committee heard was local authorities' limited freedom of movement to absorb reductions in their budget. The Committee heard that a high proportion of funding has to be spent on statutory functions and remain within service guidance. Spending reductions must therefore fall on the discretionary part of the budget, that is either spending above the statutory minimum or which is totally discretionary. The Committee heard this is around 25 per cent of local authorities' budgets. Often, these will be areas which can contribute to the longer-term health and well-being of the public, for example environmental health and leisure centres. The Committee heard that cutting these preventative services being cut to greater longer-term costs, and the Auditor General's report on environmental health set out in some detail how statutory obligations were being met currently but with a risk that performance may soon be threatened.
7. It would be helpful to hear whether you agree with local authorities' sense that a high proportion of their funding is 'ring-fenced', and set out your



assessment of the proportions of local authorities' budgets that are committed to statutory responsibilities or Welsh Government policy priorities and that which is not 'ring-fenced'. Given the high proportion of budgets that is non-discretionary, it would be helpful to understand whether the Welsh Government makes any assessment of where reductions are likely to fall, and of the longer-term consequences?

8. As a related issue, the Committee heard that there would be advantages to reducing the administrative cost associated with local authorities receiving a number of small grants, which could be dealt with more efficiently via the Revenue Support Grant. This is consistent with the Committee's discussions with the Permanent Secretary on the Welsh Government's management of grants more generally, where the Committee has welcomed action to rationalise grants. It would be helpful to understand how you are responding to these concerns with a view to reducing the cost of administration.
9. Environmental health was also discussed by the Committee as an example of where the level of required technical expertise is at odds with moves toward generalist officers. In addition, there was some concern by one local authority leader whether councillors could currently securitise the exercise of environmental health responsibilities. In his more recent report, the Auditor General sets out that the level of financial scrutiny and challenge as varying across councils, and your letter of 14 May 2015 agrees the importance of councillors' ability to challenge and scrutinise efficiency and savings plans. We would be grateful if you could set out how you are monitoring councils' uptake of the support for scrutiny you set out in your 1 July 2014 letter and seeking to ensure that weaker scrutiny is tackled.

## **Reserves**

10. The Committee was struck by the inconsistent use of cash reserves by local authorities. We heard that local authorities had been able to add to their reserves in recent years, in addition to making efficiency savings, which could now be drawn down in response to declining budgets. Of course, using reserves to mitigate against the effects of reducing budgets is only



sustainable where used to support investment to achieve longer-term savings.

11. The local authorities we spoke to on 25 November believed there was a misperception that they have a great deal more reserves than was available to them. It was asserted that there was limited flexibility for use of reserves held, given that much of their useable reserves were earmarked for specific purposes, for example the 21<sup>st</sup> Century Schools programme. The Committee heard that they had been asked to provide an outline of their level of reserves to the Welsh Government in October, and we would be grateful to understand what use had been made of this information and how it can be used to ensure the discussion around financial challenges facing local government will be well-informed.
12. The local authorities appeared to have a misunderstanding of the role of the Auditor General in relation to their reserves, believing he would raise concerns at inappropriately high levels of reserve rather than just when they are overly low. It was clarified in our evidence session that the primary focus of the Auditor General is on the accounting treatment of reserves, although he might comment if there was a risk of reserves being too low to meet future liabilities. The evidence session did highlight that some local authorities were under the impression that a clean bill of health on their accounts implied an independent endorsement of their levels of reserves.
13. Noting that the WLGA had produced a briefing on local authority reserves in November, the local authorities that appeared before the Committee welcomed the notion of further guidance on the use of reserves from the Welsh Government. Given the emphasis placed on a comprehensive strategy on reserves in your 14 May letter, we would be grateful if you could set out where you believe guidance would be helpful in terms of supporting the transparency, scrutiny and member understanding of the need for reserves and how they feature in Medium Term Financial Plans, and whether you intend to produce such guidance.



## Public engagement

14. The Committee discussed with local authorities how they engage with local communities on how budget reductions would be accommodated, including greater visibility for local authorities' cabinet members, use of focus groups and roadshows.
15. We heard that, while consultation had a limited impact on how councils' planned to respond to reductions, it could allow the authority to understand better the likely implications of any change, and allow it to be introduced more sensitively or adapt how services were delivered to realise savings. Consultation also helped set out to the public why a change was necessary, despite their reluctance to accept any reduction of service.
16. We heard examples of good practice, and believe there is opportunity for examples of good practice to be collated and shared between local authorities. We would be grateful for your views on how the Welsh Government is supporting the identification and sharing of best practice as you indicated you would be in your 22 July 2014 letter.

## Uncontrollable budget pressures

17. The Committee heard that local government does look to plan for coming years on the basis of rejected settlements, and the likely demand on their expenditure. Increasing pressure on expenditure would include rising costs of providing existing services, and costs associated with additional obligations placed on local government. The Committee heard that the local government sector works towards a shared understanding of future pressures, particularly through the Welsh Local Government Association, in addition to their own forecasts of local pressures – for example, from an aging population locally.
18. We would be grateful if you could set out how the Welsh Government assists local government in developing a sound understanding of the likely pressures in coming years, including inflation, wage inflation, and any additional statutory responsibilities.



## Funding formula

19. We noted in your letter of 1 July 2014 that the Welsh Government saw the process of reaching a Local Government settlement as being “one of the most extensive collaborative processes within government”, including though the Partnership Council, and the Finance and Distribution Sub Groups. When leaders of local authorities appeared before the Committee in November, they set out that the funding formula for local government was not well understood. In addition, we heard from Gwynedd the cost implications of delivering services in deep rural areas. Given that officials discuss the formula in detail in the Distribution Sub Group, is it likely that specific cost-incurring characteristics, such as deep rurality, that only affect some authorities would be given appropriate weight in a subgroup comprised of many authorities?
20. It would be helpful to understand whether you are satisfied that local government appreciate the collaborative process you set out as well as the Welsh Government does, and how you are confident that the collaboration allows the best decisions on allocations to be made, rather than the decisions that most readily find consensus.

## Early Departure Schemes

21. On 21 April, the Committee took evidence from Rhondda Cynon Taf and Powys county councils in response to the Auditor General’s report *Managing Early Departures Across Public Bodies in Wales*. The Committee has discussed this issue with other public bodies, and will do so again in the autumn, during its scrutiny of accounts.
22. The Committee heard that the local authorities had run early departure schemes as part of a more broad effort to reduce the cost of staffing, which was a high proportion of councils’ budgets. The Committee asked the authorities whether they had made decisions on staff departures on the basis of the requirements of a new structure, or if their restructuring followed a



departure scheme that could have included staff with skills and experience now required – meaning some departed staff needed to be replaced. The authorities we heard from were confident that they had made sound decisions on who could be released, though noted that budget reductions had to be absorbed often more quickly and at a quicker pace than was comfortable. The Committee had some reservations on whether authorities were actively redesigning their workforce and then determining who would be required to support it and whether the urgency of decision-making reduced its quality.

23. The Committee heard that councils had not received guidance from the Welsh Local Government Association on good practice for their voluntary exit schemes, including length of time before possible re-appointment, limits on severance packages, and public disclosure of settlement agreements. It would be particularly helpful if local government did not create further future challenges by making decisions on the pension arrangements for departing staff that would create pressure on local government pension funds. Given the Welsh Government's acceptance of the Auditor General's recommendation that you work with local government to seek agreement on common principles to underpin any future departure arrangements arising from local government mergers, it would be helpful if you could set out what action the Welsh Government has taken in this regard.
24. The Welsh Government's response to the Auditor General's report also mentioned the Public Service Staff Commission taking a role in coordinating early departure schemes between authorities in advance of local government reorganisation. The local authorities the Committee heard from were supportive of this suggestion, though this should allow for local variations where required. It would be helpful if you could set out what the Welsh Government's expectations are in respect of the balance between local flexibility and national consistency.
25. An issue that was discussed in this was the relatively high number of mutually-agreed departures from Rhondda Cynon Taf by staff on long-term sickness absence that were classed as early departures. Given the Committee heard that Rhondda Cynon Taf and the Wales Audit Office discussed whether



to record this information as part of the Auditor General's study of early departures, other local authorities may not have presented equivalent information as part of this exercise. It is therefore difficult to understand whether the financial challenges faced by local government has exposed deficiencies in the management of sickness absence, which these mutually agreed departures of staff with long-term sickness absences could reflect. It would be helpful if you could set out how the Welsh Government is monitoring and showing leadership in relation to sickness management, particularly through the Public Services Leadership Group.

### **Local Government Reorganisation**

26. Decisions on the future structure of local government in Wales loom large on the horizon. While the Committee did not consider the policies of the Government in respect of local government reorganisation, the current uncertainty around reorganisation and how reorganisation would be funded has had a clear impact on local authorities' ability to plan for the future. As you state in your 14 May letter, strategic financial planning and a robust medium-term financial plan are key for councils' resilience in the future.
27. The Committee discussed regional delivery of specific services, such as libraries, with local authorities and heard that, while it was possible, there was insufficient motivation to do so at the moment. This response was possibly in the context of more fundamental changes on the horizon.
28. The Auditor General's recent work on financial resilience of councils in Wales has drawn on the recent work of Grant Thornton on English councils. That showed English local authorities had been better able to respond to the challenges posed by budgetary reductions, and plan for the future in a more robust way than their counterparts in Wales. His follow-up work in the current year will allow more direct comparisons to be drawn, and the Committee will be keen to understand the extent to which uncertainty over authorities' futures has inhibited their longer-term planning. We would be grateful for any observations you have in this regard.





29. As an additional point, the Committee heard how the savings made by councils were on a recurring basis, and that the changes to how they delivered services were not temporary responses to the current challenges. This would have an implication for how medium-term costs of local government restructuring and longer-term savings would be forecast – given that the current position is not static. It would be helpful to understand how you are taking account of local authorities’ response to the current financial challenges as you progress the Government’s agenda of local government reorganisation.

Yours sincerely,



**Darren Millar AM**

**Chair**

