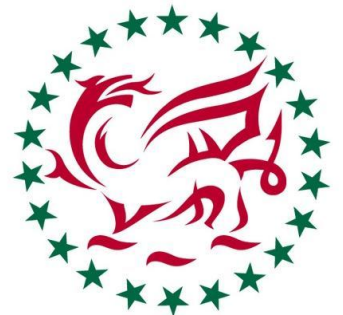




Welsh Government draft budget proposals for 2015-16

16 September 2014



WLGA • CLILC

Introduction and Context

1. The WLGA represents the 22 local authorities in Wales while the three national park authorities and the three fire and rescue authorities are associate members. It seeks to provide representation to local authorities within an emerging policy framework that satisfies the key priorities of our members and delivers a broad range of services that add value to Welsh Local Government and the communities they serve.
2. There is no escaping the impact that the current period of austerity is having across the public sector in the UK. It is clear that local government across the UK has been forced by Government to make the most difficult decisions of any part of the public sector.
3. Despite the welcome upturn in the UK economy, the impact on the public sector looks set to continue for some time since as the Welsh Government itself states in the recent "Reforming Local Government White Paper" that "even the most positive forecasts estimate that public expenditure will not return to pre-2011 levels until around 2022."
4. There are also a range of circumstances that coalesce to form an extremely uncertain future, with the Scottish referendum in September, the general election in May 2015 and differing views on the future organisation of local government in Wales all impacting in some way on strategic service delivery planning within local authorities.

Q1. The impact of the 2014-15 Welsh Government Budget

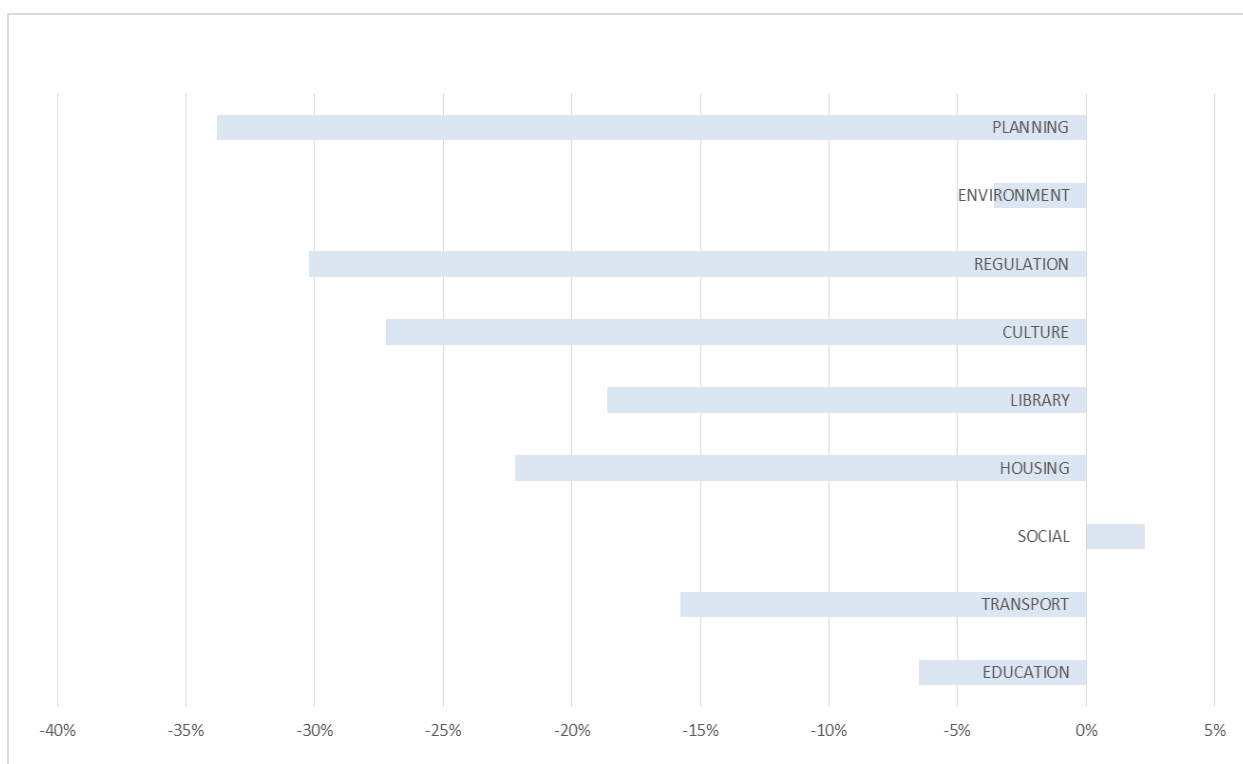
5. The current financial year was the last year of the 2010 Spending Review period. As the WLGA pointed out to the Finance Committee last year, councils had been planning 0.5% increase in core funding consistent with the forward indications published in 2011. The Minister wrote to Leaders in May 2013 warning that indicative figures were no basis on which to plan. When the draft budget and settlement were announced the eventual published reduction of 3.4%¹ in core funding equated to a reduction of £148.5 million in grant.
6. Coupled with unavoidable increases in expenditure such as the need to ensure adequate funding within schools' budgets and increased demand in social services, this led to Councils needing to find around £280 million in savings, despite an average council tax increase of 4.2%.
7. The impact of the 2014-15 budget decision should not be seen in isolation. In 2012 the WLGA commissioned the Institute of Fiscal Studies (IFS) to assess the future

¹However, on a like for like calculation, the reduction was actually 3.9% due to the inclusion within the RSG of ongoing additional funding for the council tax reduction scheme which was treated as "growth" by Welsh Government.

prospects for local government expenditure in Wales² and this analysis was adapted for their work with Wales Public Services 2025³.

- At the time the IFS estimated that in the early years of the austerity programme of the UK government, local government spending had been falling in real terms. They estimated that spend from 2009-10 up to 2012-13 had fallen by around 7.3% in Wales (half the reductions experienced in England) and analysed spending on a service by service basis. Extending this analysis for the latest data available is set out in figure 1 below.

Figure 1: Real terms change in service spend between 2009-10 to 2014-15



Source: IFS, WG RA returns 2014, HMT GDP deflators 2014 (Q1)

- Only expenditure on social services has shown a real terms increase since the onset of austerity. Despite protection for education, expenditure has fallen by 6%. The most likely explanation is that education spending outside Individual Schools Budgets is taking a disproportionate share of funding reductions coupled with the fact that the protection itself is pegged to below inflation changes to the WG budget.
- Spending on Environmental services has dropped 4%. This covers a number of spend areas including street cleansing and flood defence, however over 80% of this spend is on waste services including recycling.

² [Local Government Expenditure in Wales: Recent Trends and Future Pressures. IFS \(2012\).](#)

³ [Scenarios for the Welsh Government Budget to 2025-2026. IFS \(2013\).](#)

11. Spending on Transport shows a decline of 16%. Although expenditure in this area accounts for around 5% of local government spend, this type of infrastructure spend is most closely associated with economic growth. Indeed spending in two other areas that are most closely associated with economic development reinforce the proposition that the economic recovery may be hampered by extreme disinvestment in this area. Expenditure on planning and economic development is down 34%, and spending on non-HRA housing services is down 22%. As the Finance Committee highlighted in its report on the draft budget for 2014-15⁴ last year "...there is a disconnection between the WG's stated priorities – jobs and growth – and a budget whose clearest priorities are indicated by directing additional money towards the health service."
12. Other areas of spend also covered in figure 1 relate to cultural expenditure (including sports and leisure) and libraries. Since 2009-10, the former has reduced by 27% and the latter by 19% in real terms. These are the only two areas of service expenditure that have now dipped below spending levels in 2001-02 when adjusted for inflation. Spending on regulation is down by 30% and along with sports and leisure, might be considered areas of spend that are preventative.
13. Clearly, with reductions of this magnitude, to describe these as efficiencies or isolated cuts is an understatement. Services are being hollowed out. Spend in these areas attracts a lot of attention from Assembly Members and various Commissioners because they are valued by the public. The Joseph Rowntree Foundation⁵ has shown that many of these 'other' services are relied upon by vulnerable groups. They also prevent negative social outcomes driving demand in other budgets including the NHS⁶.

Local Government Performance

14. Local Government Performance data for 2013-14 was recently published by the Data Unit⁷. The service headings broadly correspond to those in figure 1 above. Table 1 below shows how those services performed in 2013-14 compared to 2012-13. At a Wales level, 70% (31) of the 44 indicators which are comparable between 2012-13 and 2013-14 show improvement. The gap in performance (between the best and worst performing authorities) narrowed in 59% (26) of the indicators. For 43% of the indicators, performance improved and the gap between the best and worst performing authorities narrowed.

⁴ [National Assembly for Wales \(2013\). Scrutiny of Welsh Government Draft Budget 2014-15, page 5.](#)

⁵ [JRF \(2013\). Coping with the cuts? Local government and poorer communities.](#)

⁶ [Office for Disability Issues \(2007\). Implications for health and social care budgets of investment in housing adaptations, improvements and equipment: a review of the evidence.](#)

⁷ [Local Government Performance 2012-13. Data Unit \(2014\)](#)

Table 1: Local Government Performance 2013-14

<i>Service Area</i>	<i>No of comparable indicators</i>	<i>% of indicators where performance improved</i>	<i>% of indicators where the gap narrowed</i>	<i>% of indicators where performance improved and the gap narrowed</i>
Education	11	82%	64%	55%
Social Care	20	60%	60%	40%
Housing	3	100%	67%	67%
Environment & Transport	6	83%	50%	33%
Planning & Regulatory Services	2	50%	50%	50%
Leisure & Culture	2	50%	50%	0%
Overall	44	70%	59%	43%

Source: Data Unit (2014)

Q2. Concerns about the Indicative 2015-16 Welsh Government Budget

15. Our major concern is the inability to rely on indicative figures while attempting to introduce significant reductions in funding in a planned and rational way based on sound evidence and with an appropriate lead-in time. At the time of the 2014-15 budget publication last year the forward plans for LG spending showed a reduction in core funding of 1.55%. The former Local Government Minister has again indicated that we cannot use this figure for forward planning and the reduction could be as high as 4.5%. The Welsh Government approach to forward planning has now departed significantly from the approach it took to multiyear settlements in the past. This had provided the basis for sound medium term financial planning since 2008.
16. Other concerns raised in our evidence to the Finance Committee last year remain, including the continuation of a centralised approach to funding which manifests itself through continued use of specific grants and the protection of certain service budgets.
17. There are significant concerns about the sustainability of services that are funded by specific grant, especially concessionary fares, sustainable waste management grant and supporting people. Announcements around specific grants tend to be late in terms of financial planning, close to or actually within the financial year in question. Even more worryingly, some grants such as some education grants are subject to in-year reductions in 2014-15. Again this comes back to sustainable financial planning. As the National Union of Teachers' recently pointed out⁸ "The Welsh Government talks of three year budgets but this one has barely lasted six months."

⁸ [NUT Cymru \(2014\). Press Release: Robbing Peter to Pay Paul.](#)

18. The OECD recently pointed out⁹ that the whole approach of specific grants in education “*can create confusion, be unsustainable in the long term...*”. The OECD state that this is contributing to a fragmented to approach to educational improvement and question whether this is conducive to the schools own financial planning.

Q3. Expectations of the Draft 2015-16 Welsh Government Budget

19. The majority of Councils used the Indicative Settlement reduction of 1.55% in medium-term financial plans until the Minister wrote to Leaders again stating that published indicative allocations were subject to change. This is likely to have a drastic effect on local government budgets as Welsh Government is now suggesting that the reduction could be as great as 4.5% taking an additional £120m out of core funding. The impact nationally is set out in the model at Appendix 1.

20. The table shows that if education protection continues and social care pressures cannot be ameliorated through demand management then, nationally, Councils could be facing a cumulative shortfall by 2017-18 that could fall anywhere between £600m and £900m. For 2015-16, this will mean reductions of anywhere between 13% and 25% on ‘influenceable’ budgets. These are similar reductions to those experienced in 2014-15 and will certainly exacerbate the reductions in specific areas of service spend set out in Figure 1.

21. These are not abstract calculations, as local government leaders have pointed out in a recent letter to all AMs, MPs and MEPs. Figure 2 below takes a sample of four councils across Wales: one city, one rural, one Valleys and one urban north Wales. After protections are applied the impact is stark.

Figure 2: Impact of published indicative reduction of -1.5% and further reductions of -4.5%

	CARDIFF £m	TORFAEN £m	POWYS £m	FLINTSHIRE £m
Net Base Budget 2014-15	574.0	169.0	242.4	253.7
Budgets from which savings cannot be made (e.g. Delegated Schools budgets; CTRS)	270.0	56.0	87.0	94.6
Budgets outside of Specific directorate control (e.g. Debt financing costs etc)	76.3	22.0	40.3	21.6
Budgets to which reductions can be applied (includes Social Services)	227.7	91.0	115.1	137.5
Impact of reduction of 1.5% of AEF	-4.4	-1.4	-1.8	-2.0
Unavoidable additional financial pressures	-25.5	-8.4	-8.6	-11.9
Total reductions required	-29.9	-9.8	-10.4	-13.9
Reductions (@1.5%) as a % of unprotected budgets	-13%	-11%	-9%	-10%
Further impact of funding reductions up to -4.5%	-15.2	-4.6	-6.4	-6.7
Reductions (@4.5%) as a % of unprotected budgets	-20%	-16%	-15%	-15%

⁹ [OECD \(2014\). Improving Schools in Wales: An OECD Perspective.](#)

22. This clearly shows that under the published reduction of 1.5%, councils need to find savings of between 10% and 13% from unprotected budgets. Further reductions of up to 4.5% will now require savings of between 15% and 20%.
23. There are some positive aspects to council finances next year. Due to the consistent lobbying efforts of the WLGA, the WG and UK Government agreed last year to draw to a close the complex and archaic arrangements involved in funding the Housing Revenue Account. From April 2015, the government will put in place a self-financing arrangement whereby the 11 authorities with retained stock will buy themselves out of the HRA subsidy system. These authorities will be able to retain all their rental income which will allow them to consider additional borrowing
24. The borrowing will allow those that have not already done so to reach WHQS by 2020 and will also allow for some new build and reconfiguration. This is a win-win for the Welsh Government and councils. The only negative aspect of this is that the UK Government will be introducing a borrowing cap that will restrict the extent to which new build can place, a policy inconsistent with the rules that govern councils' ability to borrow on the general fund through the prudential system.

Future Financial Planning

25. The WLGA has worked with the LGA to find good practice over the border and many councils in Wales are speaking to their English counterparts directly on approaches to operational efficiency and concepts such as Co-operative Councils or Commissioning Councils. While transformational and transactional efficiency continues to make a contribution to budget shortfalls in England, the LGA report that 9 out of 10 councils in England are undertaking following activities:
- Reducing overall staff numbers
 - Delivering some services more efficiently
 - Reducing or restructuring the senior management team
 - introduced or increased charges for services
 - new service delivery arrangements with other public bodies
 - renegotiated existing service delivery contracts
26. The approach being taken in England by the UK Government is raising the spectre of comprehensive service failure by 2017-18. A recently published report by PwC¹⁰ concluded that more than half of council leaders in England believe some local authorities will fail to deliver the essential services residents require within the next year as the impact of government spending cuts increases.
27. Here in Wales, councils' own medium-term financial planning should be flexible enough to cope with uncertainty under differing assumptions. However the key

¹⁰ [PricewaterhouseCoopers LLP \(2014\). Local State We're In 2014.](#)

variable in the funding equation is RSG from the Welsh Government. All the indications are that 2015-16 will be the third year in a row that the published indicative settlement has been revised downwards in a way that makes sound financial planning untenable.

Q4. Specific Areas in Scrutiny of the Budget

a) Preparation for the Wales Bill

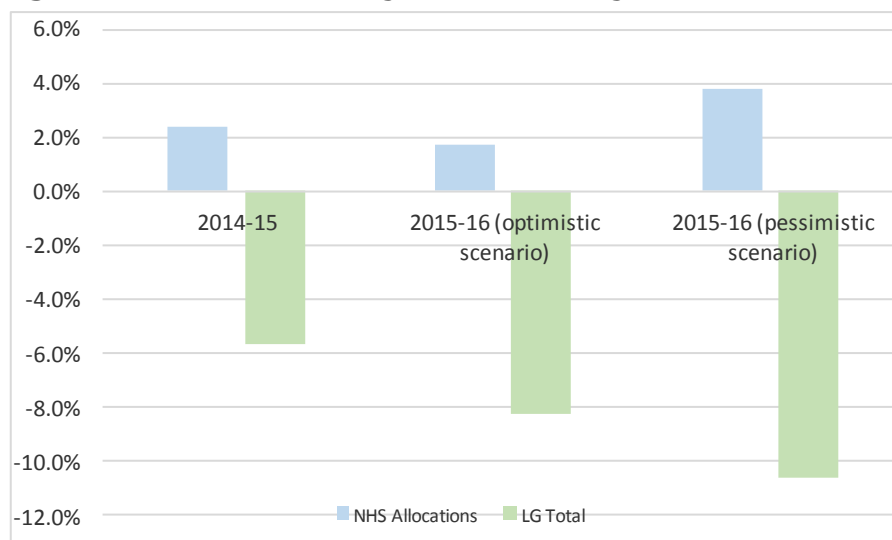
28. While there are limitations within the Wales Bill, it is important to recognise the potential opportunities afforded to the National Assembly for Wales and the Welsh Government, coupled with greater responsibility and accountability.
29. Undoubtedly, the devolution of tax and borrowing powers will increase the autonomy of the Welsh Government and provide greater levers through which to influence public policy, spending and economic growth in Wales. However, given its experience of late notice of significant reductions in indicative budgets, local government is extremely concerned about the impact of the potential for increased volatility within the Welsh Government's budgets.
30. Local government is the only part of the public sector to raise taxes within Wales currently and we are pleased that we can now share that expertise through the Welsh Government's Tax Advisory Group. As Gerald Holtham pointed out in a recent paper to the Institute of Welsh Affairs (IWA) "Taxation in Wales". It is crucial that the taxes already raised and collected within Wales are considered alongside the newly devolved taxes in an integrated way.
31. Local government would expect to be engaged and consulted on the full range of changes to be introduced in the Wales Bill, given its role within the constitutional arrangements in Wales.

b) Local health board financial arrangements

32. In the letter warning of changes to indicative plans back in June, the former Local Government Minister makes it clear that pressures in the NHS underpin the Welsh Government's decision to revisit the indicative plans for 2015-16. This was also the reason cited in the Education Minister's letter signalling in-year cuts to some education grants.
33. The Nuffield Trust study cited by the Welsh Government sets out demographic and unavoidable financial pressures that they are prepared to fund. However local government is now expected to absorb similar pressures within its own reducing budgets. This is a clear signal that local government services and employees now play second fiddle those of the health sector.

34. Demographic pressures within social services budgets are exhaustively documented in the work of Wales Public Services 2025¹¹ and are estimated to contribute pressure of £49m in 2015-16, rising to £97m by 2016-17 according to the table in Appendix 1. Other pressures cited in the Nuffield report apply equally to local government – price inflation, pay claims, changes in employer pension contributions and future pressures due to the introduction of the single tier pension. These will add £76m in pressures in 2015-16, rising to £225m by 2016-17.
35. Figure 3 below sets out in stark terms the differential treatment between health and local government in terms of funding. Such circumstances make it incredibly difficult for local government to engage with their local health boards on an equal footing. Between 2009-10 and 2014-15, funding for local government (specific and general grant) has reduced by 6% while funding for the NHS has increased at 2% in real terms.
36. In 2015-16, based on the current indicative allocations, NHS funding dips to just below 2% while local government funding will 8%. If the worst case scenario plays out, and more general grant is taken from local government is transferred to the NHS, then the local government will have absorbed real terms funding reductions of over 10% while the NHS will have experienced increases of around 4%.

Figure 3: Real terms change in WG funding for LG & NHS since 2009-10



Source WG Budget 2009-10, WG Budget 2014-15, LG Settlement 2009-10, LG Settlement 2014-15, HMT GDP deflators, (2014, Q1)

37. Inequality in the responses to the pressures facing local services, including social services, compared to health services is contributing to the difficulties facing the Welsh public sector. Finances are continuously channelled towards meeting the costs of current arrangements rather than being invested in innovative ways of delivering services as a whole, and implementing preventative measures in a holistic way.

¹¹ [Wales Public Services 2025 \(2013\). Future Pressures on Welsh Public Services: Financial Demand and Other Cost Pressures to 2025 and a Review of Potential Responses.](#)

c) Approach to preventative spending and how is this represented in resource allocation

38. As described in the WLGA's evidence to the Finance Committee last year there is a considerable body of evidence that demonstrates that the right intervention at an early enough stage across the early years, health, social care and criminal justice system can significantly diminish the need for more costly interventions in later life. The difficulty is to find the additional investment required to introduce these measures at a time of financial austerity while still managing to provide existing demand.

39. While there are a number of preventative policies that have been introduced by Welsh Government there remains a lack of a strategic approach to these that could yield the greatest results. Appendix 2 sets out some barriers to moving to a preventative approach to public service delivery that have yet to be addressed effectively.

d) Impact of the Welsh Government's legislative programme and whether its implementation is sufficiently resourced

40. In our experience, while local government and the WLGA are often involved in and consulted with during policy development, insufficient resource and effort is put towards ensuring a robust financial impact assessment process is undertaken and even where attempts are made to undertake such assessments, it is often late in the day and rushed. In our view, the best results are achieved where there is early collaboration in identifying and investigating the full implications of policy changes and a shared understanding of any potential costs and savings.

Conclusion

41. The combined impact of austerity and increasing demand is biting deeper into local public services. A lack of certainty around Welsh Government plans and flexibility in our own funding arrangements are hampering our attempts to undertake robust financial planning for the medium to long term. It means that managing budget reductions and transforming services cannot be done in an appropriately timely way.

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Appendix 1

Around 40% of a Council budget is spent on education services which is protected and pegged to 1% above the change in the Welsh Block. For each of the future years up to 2017-18, it is assumed that the commitment on education spend remains although it is impossible to predict the WG budget beyond the current Spending Round planning horizon.

Aggregate Medium Term Financial Plan

Net Revenue Expenditure (£m)	14-15	15-16	16-17	17-18
Education	2,363	2,386	2,410	2,434
Social Services	1,392	1,392	1,392	1,392
Fixed budgets	708	708	708	708
Other	1,057	1,057	1,057	1,057
Pay Award 1% (excludes schools)		21	42	64
Employer Pensions Costs - Teachers		13	23	23
Employer Pension Costs - LGPS		9	27	27
Single Tier Pension - loss of NI rebate			67	67
Price Inflation (Contracts, fuel, utilities, business rates)		33	66	99
Demographic Pressures (WP 2025 Assumptions)		49	97	146
CTRS Pressure		10	27	45
Total Expenditure	5,521	5,679	5,918	6,063
Funding (£m)				
Council Tax @ 4%	1,256	1,306	1,359	1,413
AEF @ -1.5%	4,265	4,201	4,138	4,075
Total funding AEF	5,521	5,507	5,496	5,488
AEF @ -2%	4,265	4,179	4,096	4,014
Total funding AEF	5,521	5,486	5,454	5,427
AEF @ -3%	4,265	4,137	4,012	3,892
Total funding AEF	5,521	5,443	5,371	5,305
AEF @ -4%	4,265	4,094	3,930	3,773
Total funding AEF	5,521	5,400	5,289	5,186
Budget shortfall with AEF @- 1%		173	422	575
Budget shortfall with AEF @- 2%		194	464	637
Budget shortfall with AEF @- 3%		237	547	758
Budget shortfall with AEF @ -4%		279	630	877

Social services accounts for around 25% of net revenue spend and it is assumed that it is subject to pressures set in the Wales Public Services 2025 report of around 3-4% per annum. A further 13% of a Council's budget cannot be controlled. This includes capital charges (payments on interest and debt repayment, including PFI)

and contributions to other organisations such as Fire Authorities. It also includes areas of the budget that are demand-led such as concessionary fares and the Council Tax Reduction Scheme (CTRS). These have the potential to increase and the cost of the CTR Scheme, in particular, is highly sensitive to the level of the Council's own council tax levels and caseload.

In addition councils have to plan for pay and price inflation and changes to the tax and pensions system. Over the next two years unavoidable pressures will arise from the changes to the tax and pensions regimes – these include

- a. Increase in the employers contribution to the teacher's pension (part year increase in 2015-16 and fully impacted by 2016-17)
- b. Increase in the employers contribution for the LGPS (part year increase in 2015-16 and fully impacted by 2016-17)
- c. Loss of the National Insurance rebate for contracting out of SERPS with the introduction of the Single Tier Pension (fully impacted by 2016-17)

Auto-enrolment will also commence in 2017-18 but this is difficult estimate. Additionally, there are likely to be a number of financial implications arising from legislation. Since the demise of the Expenditure Sub Group, there appears to be little joint understanding of these financial pressures.

On the funding side, net revenue expenditure is financed from two sources: the main block grant and council tax. Council tax is assumed to grow at 4% but under the new CTRS scheme a rise equivalent to this produces an immediate pressure of £0.4m as the Council has to fund the reduction scheme for increases.

Appendix 2

Barriers to fully implementing preventative measures

Funding

- There is too much pressure on budget holders to tackle negative social outcomes here and now, despite recognition this will have limited success in the longer term. This results in difficulty in freeing up money to finance preventative spend that is currently tied up in acute care and hospital provision.
- An increase in investment of preventative spend programmes is not cost-neutral and does not mean that existing “reactive budgets” can be immediately cut;
- The public service body or sector that invests in the preventative spend may not be the same body that derives the benefits;
- Budget restraints may make a concerted focus on preventative spend less likely.

Impact and Evaluation

- Given the nature of preventative policies, there is a significant time-lag between their implementation and the ability to provide clear evidence of their impact. It may be difficult to prove that a specific intervention was responsible for an outcome;
- The longer-term outcomes delivered by preventative spending measures may be difficult to evaluate.

Political and Financial Cycles

- The political cycle every four years means that some preventative spend projects may come to a premature end as they need to run for longer time periods in order to deliver results;
- The annual budget and funding cycles, sometimes with 2-3 year forward indications, do not provide enough certainty of investment for projects that need to be implemented consistently over a long time-frame