

**Audit Scotland report:****Local government in Scotland: Financial bulletin 2022/2023**

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**Date of meeting** 23 February 2024**Date of report** 1 February 2024**Report by Chief Executive****1. Object of report**

To advise the committee on the issue of an Audit Scotland report titled '*Local government in Scotland: Financial bulletin 2022/23*' and outline the key messages and implications for SPT contained therein. Members are reminded that the full report was emailed separately.

**2. Background to report**

The report says that Scotland's councils are managing their money effectively, increasing reserves, with longer-term financial plans in place. Whilst no council was at immediate financial risk in 2022/23, there is no certainty this will continue. This makes an agreement between the Scottish Government and councils to secure a sustainable, longer-term funding arrangement to deliver local services all the more urgent.

The report adds that effective financial management within councils is crucial as budget gaps increase. Councils continue to rely on savings and reserves to balance budgets. Over half of councils used financial flexibilities in 2022/23. This helps with immediate budget pressures but defers costs to later years and fails to tackle underlying challenges to financial sustainability.

The Accounts Commission's latest report assesses the financial position of Scotland's councils during 2022/23 and the outlook for services beyond this. While councils received more funding and income in cash terms in 2022/23, high inflation means this fell by nearly three per cent in real terms compared to the previous year. A significant and increasing amount of funding continued to be either formally ringfenced or directed towards specific services and national policy objectives – reducing councils' flexibility in using money to meet local needs.

Despite more core funding from the Scottish Government for 2023/24, there was a significant increase in councils' total funding gap, due to pressures including increased demand for services, inflation and the cost-of-living. Capital budgets were also significantly strained, risking knock-on impacts on the maintenance of key public buildings and infrastructure, for example schools, libraries and roads.

Councils recognise the risks ahead, but they need to innovate at pace and make difficult decisions about cuts to services to remain financially sustainable. Some councils have experienced opposition from within their communities when seeking to reduce services to

balance budgets. This reinforces the need for frank consultation and engagement with communities when planning change.

The Audit Scotland report can be found at: [https://www.audit-scotland.gov.uk/uploads/docs/report/2024/nr\\_240116\\_local\\_government\\_finance.pdf](https://www.audit-scotland.gov.uk/uploads/docs/report/2024/nr_240116_local_government_finance.pdf)

### 3. Outline of proposals

The report outlines the following key messages:

#### *Funding and outturn in 2022/23*

1 Despite councils receiving more funding and income in cash terms, due to high inflation in 2022/23 total revenue funding from all sources fell by £619 million (2.8 per cent) in real terms to £21.3 billion compared to 2021/22.

2 Councils received more core revenue funding from the Scottish Government than in 2021/22, rising from £12.1 billion to £12.2 billion (0.7 per cent) in real terms. However, an increasing proportion is ring-fenced or provided with the expectation it will be spent on specific services. This means that the amount of funding available for councils to spend freely on local priorities is reducing. There are commitments in the Verity House Agreement to move to a default position of removing ring-fencing or direction of funding wherever possible.

3 There is pressure on all public-sector capital budgets, and this presents risks to the viability of local government capital programmes, many of which impact on key services (e.g., the construction and maintenance of schools, libraries, roads). Capital funding from the Scottish Government rose in 2022/23 but remains lower than before the pandemic and has been volatile over the past decade. Driven by increased borrowing councils' capital expenditure increased in 2022/23 by 16 per cent in cash terms to £3.6 billion. Borrowing costs have reduced in recent years as many councils have used permitted financial flexibilities to reprofile debt payments. While helping with immediate budget pressures, these decisions defer costs to later years and do not tackle the underlying challenges to financial sustainability. Additional borrowing also places further pressure on revenue budgets over the longer term.

4 At the time of setting their 2022/23 budgets, councils anticipated budget gaps of over £476 million for the year, higher than the previous year. Councils are increasingly having to rely on savings and reserves to balance budgets. Achievement of savings targets was good in 2022/23 and improved on 2021/22. Greater transparency is required in the reporting of financial outturn in council accounts, including savings performance. This transparency and timely public engagement are essential as councils make increasingly difficult decisions to reduce or stop services to help balance budgets.

#### *Councils' financial position and outlook from 2023/24*

5 Despite the financial pressures of recent years, half of councils increased their usable reserves in 2022/23, and overall usable reserves grew to £4.45 billion. This is driven by growth in committed reserves. Some of this is remaining Covid-19 funding, some is attributable to the permitted use of financial flexibilities for the repayment of longer-term debt but there are also indications councils are building up reserves to manage the known financial challenges in future years. However, the lack of transparency in some councils' annual accounts makes it difficult to draw firm conclusions on councils planned use of reserves.

6 Local appointed auditors did not identify any councils in Scotland as being financially unsustainable in the short term. However, the financial outlook is extremely challenging with Scottish councils facing unprecedented financial and service demand pressures which present real risks for the future. Although Scottish Government core funding increased in cash and real terms in 2023/24, councils reported a significant increase in the total budget gap to £725 million.

7 Councils' medium- and longer-term financial plans demonstrate a clear recognition of the difficult financial context and the need to continue to innovate at pace and make difficult decisions to become more financially sustainable. But some councils are already experiencing significant resistance when seeking to make service reductions to balance budgets. This reinforces the need for effective consultation and engagement with communities on planned local service changes.

8 The Verity House Agreement includes a commitment to offer councils longer-term funding and greater local financial flexibility. These proposed changes will be important, in providing greater financial certainty to support better long-term planning and more flexible direction of resources to meet local need. However, the recent announcement of a proposed council tax freeze significantly reduces discretion and flexibility at individual council level. The impact this will have on financial sustainability is not yet known, but councils have placed an increased reliance on raising council tax to help deliver a balanced budget over the past two years.

#### Recommendation(s) outlined in the report

##### *Councils should:*

- Prioritise the achievement of recurring savings and avoid reliance on non-recurring savings to enhance longer-term financial sustainability;
- Ensure that management commentaries are open and transparent, include a clear link between budget outturn and the financial performance in the accounts and report on the achievement of planned savings targets;
- Provide clear statements about reserves policy and explicitly set out the purpose of committed reserves within their annual accounts. This will enhance the level of assurance that councils can provide regarding their ongoing financial sustainability;
- Ensure effective and timely consultation and engagement with communities on the options that must be considered to achieve a balanced budget;
- Strengthen their monitoring and reporting of financial resilience including clearer and more public-facing use of performance against financial resilience indicators and measures. Financial resilience indicators should be a component of councils' medium and longer-term financial plans to provide assurance that they are balancing short-term pressures with robust planning for long-term financial sustainability;
- Work with the Scottish Government to build momentum and accelerate progress in the development of a fiscal framework for local government to enhance the clarity and certainty of budgets for councils in future years.

#### **Implications from the Audit Scotland report key messages**

Councils in the Partnership area fund SPT's revenue budget.

SPT has and continues to face similar challenges as set out in the report.

The key messages also apply to service provision.

#### 4. Committee action

The Committee is asked to note the contents of this report and the Audit Scotland report titled '*Local government in Scotland: Financial bulletin 2022/2023*'.

#### 5. Consequences

Policy consequences	<i>None.</i>
Legal consequences	<i>None.</i>
Financial consequences	<i>None.</i>
Personnel consequences	<i>None.</i>
Equalities consequences	<i>None.</i>
Risk consequences	<i>None.</i>
Climate Change, Adaptation & Carbon consequences	<i>None.</i>

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