

Report

Report to:	Risk and Audit Scrutiny Committee
Date of Meeting:	18 June 2020
Report by:	Executive Director (Finance and Corporate Resources)

Subject:	Audit Scotland – Financial Overview 2018/2019
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1. Purpose of Report

1.1. The purpose of the report is to:-

- ♦ provide the Risk and Audit Scrutiny Committee with a summary of the information contained within the Audit Scotland Report 'Financial Overview 2018/19' published in December 2019.

2. Recommendation(s)

2.1. The Risk and Audit Scrutiny Committee is asked to approve the following recommendation(s):-

- (1) that the key messages and recommendations of the Audit Scotland Overview Report 2018/2019, as detailed in sections 4 to 7, be noted; and
- (2) that the Council's position in relation to these messages/recommendations, as detailed in section 8, be noted.

3. Background

3.1. In December 2019, Audit Scotland published the Financial Overview 2018/19 report on behalf of the Accounts Commission. Audit Scotland publish two overview reports each year, this one focuses on financial matters, and the other report, on councils' performance and outcomes, is expected be published in April 2020. A copy of the [Audit Scotland - Financial Overview 2018/19](#) report can be found on the Audit Scotland website.

3.2. The Audit Scotland report is divided into 4 parts:

- Part 1: Councils' Income in 2018/2019
- Part 2: Councils' Financial Position
- Part 3: Councils' Financial Outlook
- Part 4: Integration Joint Boards' Overview 2018/2019

3.3. The key messages from each of the 4 parts are outlined in sections 4 to 7 of this report, with comments on South Lanarkshire Council's position specifically noted in section 8.

3.4. In addition to these key messages, the overview report poses a number of questions for consideration by councillors. These are highlighted in section 9, and detailed in Appendix 1 to this report, alongside the Council's position in relation to these questions.

4. Part 1 – Councils' Income in 2018/2019

- 4.1. A number of key messages are presented by Audit Scotland in their report, in relation to councils' budgets and spending in 2018/2019:-
- Scottish Government revenue funding to councils increased in 2018/2019 by 1.1% in cash terms and decreased by 0.7% in real terms. Council income grew by £0.4 billion in cash terms.
 - Between 2013/2014 and 2018/2019, funding from the Scottish Government to local government decreased by 7.6% in real terms. Funding to other areas decreased by 0.4% over the same period.
 - Council Tax changes raised an additional £97 million in 2018/2019. The increase was due to all councils choosing to increase council tax by the maximum 3% and also increases in the number of properties.
 - In order to be more transparent about how funding reflects the factors that drive demand, the Scottish Government has now provided information to individual councils on the calculations for the non-GAE distributions.
 - A growing proportion of Scottish Government revenue funding to councils is committed to national policy initiatives. This reduces the flexibility councils have for deciding how they plan and prioritise the use of funding to respond to local priorities. COSLA's view is that Scottish Government policies and fixed commitments represented 58% of local government revenue expenditure budgets in 2018/2019, rising to 60% in 2019/2020.
 - The proportion of income from each main source (General Revenue Grant, Non-Domestic Rates etc.) varies significantly across councils.

5. Part 2 – 2018/2019 Councils' Financial Position

- 5.1. A number of key messages are presented by Audit Scotland in their report in relation to the 2018/2019 Financial Performance of councils:-
- In 2018/2019, the national local authority funding gap was 3% of total budget.
 - The 2018/2019 funding gap of 3% of total budget was lower than the previous year (4%). Councils planned to manage this mainly through savings, although a shortfall in savings achieved meant that a higher proportion of the funding gap was met from reserves than was planned.
 - Scottish councils increased their use of revenue reserves, with a net drawdown in 2018/2019 of £45 million.
 - Twenty three councils have reduced their General Fund reserves over the last three years. No council is in a position where this rate of depletion would eliminate the total General Fund within three years.
 - Capital expenditure increased by £62 million (2.3%) in 2018/2019 to £2.75 billion, with more spent on housing and economic development and less spent on education.
 - The value of pension liabilities in councils increased by £0.5 billion to reflect the impact of the McCloud case (relating to transitional protection for some pension scheme members).
 - Councils should continue to improve the transparency of the management commentary included in their Accounts.

6. Part 3 – Councils' Financial Outlook

- 6.1. A number of key messages are presented in the report in relation to the Financial Outlook for councils, namely:-
- Scottish Government revenue funding to local government in 2019/2020 increased by 2.9% in cash terms (0.9% in real terms).

- In 2019/2020, the Scottish Government increased the cap on council tax increase. Twelve councils decided to increase council tax by the full amount permitted of 4.79%.
- Many councils are also seeking other ways to increase income, including increasing fees and some have introduced new charges in 2019/2020. Some councils also continue to pursue new local taxes.
- Councils' 2019/2020 financial plans identified a total funding gap of £0.5 billion (3% of income). This continues the increasing pressure on councils to find further cost savings, redesign services, reduce services, increase income or use reserves. Councils planned to manage their funding gaps mainly through identified cost savings.
- All councils have medium-term financial planning covering three years or more. Long-term financial planning has not improved since last year and more progress is required.
- The Scottish Government has made a commitment to set out multi-year budgets, which will assist councils with financial planning.
- Councils have made preparations for EU withdrawal but there are many potential implications that cannot be anticipated in financial planning.

7. Part 4 – Integrated Joint Boards' (IJBs) Overview 2018/2019

7.1. A number of key messages are presented in the report in relation to IJBs, namely:-

- The pace of health and social care integration has been too slow and there is limited evidence to suggest any significant shift in spending from health to social care.
- Overall, IJB budgets increased by 3% in 2018/2019.
- The identified budget gap reduced from £248 million (2.9% of total income) in 2018/2019 to £208 million (2.5% of total income) for 2019/2020.
- The majority of IJBs struggled to achieve break-even in 2018/2019 and nineteen would have recorded a deficit without additional funding from partners at the year end.
- Around a third of the IJBs failed to agree a budget with their partners for the start of the 2019/2020 financial year. For several IJBs, although the budget was set on time, they still had an element of unidentified savings which meant the budget was unbalanced at the start of the year.
- A focus on long-term planning is required by IJBs to assist effective decision making that will support long-term financial sustainability.

8. South Lanarkshire Council – Financial Overview 2018/2019

8.1. The Audit Scotland report contains a number of tables that set out information for all councils. For the majority of indicators, South Lanarkshire Council's results were in the main grouping of councils. However, there were three areas where the Council's results were outwith the main grouping. These are detailed below.

8.2. **Average annual movement in councils' general fund reserves over the last three years:** The Council is the second highest in terms of average annual movement in its General Fund Reserve over the last three years. The Council's General Fund Reserve has increased by an average of approximately 17%. This is mainly due to the agreed transfer to the General Fund Reserve of amounts generated through decisions made on Debt Flexibility (£18.3m). Transfers for Pupil Equity Fund and Early Years, due to timing of funding, and underspends, earmarked to be utilised in future years' strategies, have also contributed to the increase in the General Fund Reserve.

8.3. **Underlying borrowing and gross debt as a proportion of net annual revenue:** The Council is seventh highest in terms of its level of borrowing/debt required to fund

its capital expenditure, as a proportion of its net annual revenue. This is due to the successful delivery of ambitious capital programmes funded, in part, by borrowing. The financial impact of borrowing for capital expenditure has been built into the budget.

- 8.4. **Annual cost of unfunded pension benefits as a percentage of net operating expenditure:** The Council is sixth highest in terms of annual cost of unfunded pension benefits as a percentage of net operating expenditure. All councils have ongoing pension commitments arising from past decisions on early retirements.

9. Questions for Councillors

- 9.1. Throughout the Audit Scotland report there are a number questions for the attention of councillors. For each question, Audit Scotland suggests that councillors should consider 'What do I know?' and 'Do I need to ask further questions?'
- 9.2. The questions, which cover a variety of issues, are listed within Appendix 1 along with the Council's position in relation to each of the areas.

10. Employee Implications

- 10.1. None.

11. Financial Implications

- 11.1. The Audit Scotland Report raises a number of financial areas for consideration by councils, however, there are no direct financial implications as a result of the content of this report.

12. Climate Change, Sustainability and Environmental Implications

- 12.1. There are no implications for climate change, sustainability or the environment in terms of the information contained in this report.

13. Other Implications

- 13.1. There are no risk implications in terms of the information contained in this report.

14. Equality Impact Assessment and Consultation Arrangements

- 14.1. This report does not introduce a new policy, function or strategy or recommend a change to an existing policy, function or strategy and, therefore, no impact assessment is required.
- 14.2. There is also no requirement to undertake any consultation in terms of the information contained in the report.

Paul Manning

Executive Director (Finance and Corporate Resources)

3 April 2020

Link(s) to Council Values/Ambitions/Objectives

- ◆ Accountable, Effective, Efficient and Transparent

Previous References

- ◆ None

List of Background Papers

- ◆ Local Government in Scotland – Financial Overview 2018/19 - Audit Scotland, December 2019

Contact for Further Information

If you would like to inspect the background papers or want further information, please contact:-

Lorraine O'Hagan, Finance Manager (Strategy)

Ext: 2601 (Tel: 01698 452601)

E-mail: lorraine.o'hagan@southlanarkshire.gov.uk

Audit Scotland – Questions for Elected Members

Audit Scotland Questions for Elected Members	South Lanarkshire Council Perspective
<p>Income</p> <ul style="list-style-type: none"> How dependent is your council on the various sources of income compared to other councils – Scottish Government funding, grants, council tax and receipts from customers/clients? 	<ul style="list-style-type: none"> The Council, like all other councils, is dependent on a combination of the sources of income noted. The main elements, expressed as a percentage of total income are noted below. The Scotland average is noted in brackets: <ul style="list-style-type: none"> Scottish Government funding - 64% (58%) Grants - 12% (17%) Council Tax - 15% (14%) Receipts from customers/clients - 9% (11%)
<p>Council and IJB budgets</p> <ul style="list-style-type: none"> Is a budget agreed before the start of each financial year? If not, why not? How big is the funding gap for your council/IJB relative to the total budget? What are your Council's plans for meeting the current and future funding gaps – savings plans, efficiencies, reduction in services or transformation, increased charges, use of reserves? 	<ul style="list-style-type: none"> The Council budget is set and agreed before the start of each financial year. The 2020/2021 Budget Strategy identified a budget gap, before an increase in Council Tax, of £13.651m (this equates to approximately 1.8% of the Council's expenditure budget for 2020/2021). The Council will plan to meet any funding gaps from a combination of measures including savings, increased charges and the prudent use of reserves, in line with the Council's Budget Strategy.

Audit Scotland Questions for Elected Members	South Lanarkshire Council Perspective
<p>Council and IJB budgets (cont'd)</p> <ul style="list-style-type: none"> • Are there significant elements of unidentified savings in the agreed budget or are all planned savings actions clearly identified? • How well are you kept informed about progress against savings plans? • Does your council/IJB have a transformation plan? Does it clearly set out the aims and objectives and how and when these will be achieved? • How effectively are you engaged and informed about the transformation programme and kept informed about progress? 	<ul style="list-style-type: none"> • There are no significant elements of unidentified savings in the Council's budget. • Members' awareness sessions take place each year, prior to approval of the annual budget, to discuss updates on the budget strategy and proposals for savings. Ongoing monitoring of the revenue budget includes the impact of savings and their achievement. • Over a number of years, there has been an approach where, through integrated cross-Resource working, real proposed efficiencies have been identified, rather than having an aspirational transformational target. Through this process, the Council focuses on transformation and looking to maintain or improve performance, and not solely focus on savings. <p>Any Transformation plans in relation to the IJB are reported to the IJB itself.</p> <ul style="list-style-type: none"> • As noted above, the Council works to achieve real savings, rather than a transformation target. Their achievement is included in the ongoing revenue budget monitoring reported regularly to members. In addition, progress towards meeting Council objectives is the subject of regular monitoring. Reports on progress towards milestones are regularly presented to committees and the public. Where measures are not on course to be achieved, these will be referred to individual Resource Committees for consideration.

Audit Scotland Questions for Elected Members	South Lanarkshire Council Perspective
<p>Reserves</p> <ul style="list-style-type: none"> • What is the council's/IJBs reserve policy? • Do committed/earmarked/specific reserves have clear purposes and projected cash-flows or are they part of the general contingency or uncommitted general fund? • Are these commitments reviewed annually to ensure they reflect the best use of the council's/IJBs reserves? • Is the council/IJB using up its reserves and is it likely to deplete these over the medium or long term (within 5 or within 10 years)? 	<ul style="list-style-type: none"> • The Council has a Reserves Strategy which forms part of the Council's overall Budget Strategy. An annual update on the Council's Budget Strategy, as reported to the Executive Committee for approval, details the proposed use of any reserves where appropriate. Updates highlight the unsustainable nature of reserves as a funding source. <p>The IJB has its own Reserves policy which was approved by the IJB.</p> <ul style="list-style-type: none"> • All reserves are held for specific purposes. Any contribution to reserves are approved by Members after they have been provided with the rationale for their retention and use. • All committed reserves are reviewed at least annually. The position on Reserves is reported to the Council's Executive Committee as part of the year-end process. This includes the results of the review of commitments. <p>The Chief Finance Officer of the IJB reports its Reserves commitment to the IJB annually as part of the Annual Accounts.</p> <ul style="list-style-type: none"> • All earmarked reserves, with the exception of the Uncommitted General Fund and the HRA, will be utilised for earmarked purposes, over the period of the long term budget strategy. <p>The IJB Reserves will be utilised over the medium term.</p>

Audit Scotland Questions for Elected Members	South Lanarkshire Council Perspective
<p>Capital</p> <ul style="list-style-type: none"> • What are your council's medium and long term plans for capital spending? • How well are you kept informed about progress against capital plans and how well do you understand the reasons for any underspend against the annual capital budget? 	<ul style="list-style-type: none"> • The Council's plans for medium and long term capital spending are as approved in the Executive Committee Report on 21 November 2018, covering the period from 2018/2019 up to 2027/2028. • Members are updated by four weekly capital monitoring reports, presented to the Executive Committee, which detail the progress of the capital programme against budget and provide explanations for any variances.
<p>Debt</p> <ul style="list-style-type: none"> • What is your council's current debt position relative to its annual revenue? • How much of the council's budget is used to pay interest and debt repayments? • Are you given clear and sufficient information to understand risks and support decisions about future borrowing? 	<ul style="list-style-type: none"> • The Council's current gross debt as a proportion of net annual revenue is 167.2%. This is in comparison to other councils where their proportions range from 58% to 237%. The Council's level of debt reflects the successful delivery of ambitious capital programmes funded, in part, by borrowing. • The Council's loan charges budget is presented to the Executive Committee on a 4 weekly basis, reporting any anticipated variances. For 2019/2020 the budget is £53.916m. • As a matter of course, any new borrowing decisions are accompanied with information on the implications of the borrowing. Updates on the Council's Budget Strategy, reported to the Executive Committee for approval, detail the position in relation to planned capital expenditure and the Treasury Management Strategy. The updates provide information on borrowing and debt projections.

Audit Scotland Questions for Elected Members	South Lanarkshire Council Perspective
<p>Business cases for severance</p> <ul style="list-style-type: none"> Does the council prepare business cases for severance proposals and are these reported to councillors? 	<ul style="list-style-type: none"> Factors taken into consideration in any severance proposal includes the payback period for any sum due to be paid. A six monthly report is presented to the Finance and Corporate Resources Committee which includes the cost of any early retirements. A guidance document on Early Retirement and Voluntary Severance for Personnel Sections is included on the Council's Intranet. The Council's Executive Committee (12 September 2012) approved a paper agreeing the Early Retirement/Voluntary Severance process in relation to Chief Officers and Statutory Officers.
<p>Transparency in accounts</p> <ul style="list-style-type: none"> Does the management commentary of the council and IJB accounts show the outturn against budget reconciled to movement in the general fund and progress against agreed savings plan? 	<ul style="list-style-type: none"> The management commentary includes details of the annual budget, actual before and after transfer to reserves, and explanations for the transfer to reserves. Progress on achievement of savings is monitored through regular scrutiny of the overall Council budget.

Audit Scotland Questions for Elected Members	South Lanarkshire Council Perspective
<p>Financial planning</p> <ul style="list-style-type: none"> Does your council have medium and long term financial plans, and do they include a range of potential funding and financial scenarios? Does the medium-term plan provide sufficient information on estimated Scottish Government funding (or host partner funding), projected net expenditure (in total and for each service), projections for service income, projections for cost of borrowing? 	<ul style="list-style-type: none"> A Budget Strategy for 2019/2020 to 2021/2022 and a longer term outlook to 2028/2029 was presented to the Executive Committee in August 2018. Similar to previous strategies, the paper provided commentary and assumptions, where possible, including assumptions about demographics, economic conditions and inflation. The Budget Strategy (as referred to above) includes government grant scenarios, borrowing and debt projections and identifies the resultant potential savings requirement, at Council level, over the term of the Strategy. One of the main budget assumptions is the level of government grant. In recent years, scenarios have focussed on the level of funding reductions. This has formed an integral element of the medium term budget process. The Council's new longer term Strategy (August 2018) expands this scenario further to reflect changes to social care demand, as well as other key areas of budget pressures. In arriving at the expenditure assumptions within the Budget Strategy, a number of factors are taken into account, including investments in Council Priorities, and the impact of changing demographics. Investments in services, or projected movements in service income are considered in the Budget Strategy. The Strategy also considers the impact of borrowing. National pay negotiations for all employees continue to be a significant element of the budget investments required.