

**Accounts Commission: Local Government in Scotland:
Financial Overview 2019/20 (January 2021)**

Report by Gary Fairley, Chief Officer Corporate Solutions

Report for Information

1 Recommendations

The Committee is asked to note the Accounts Commission report and the position of Midlothian Council in relation to the report's key messages.

2 Purpose of Report/Executive Summary

To provide Audit Committee with a summary of the Accounts Commission report, 'Local Government in Scotland: Financial Overview 2019/20' and the Council's position in relation to the report's findings. The full report can be accessed on the Audit Scotland website by following this link:

<https://www.audit-scotland.gov.uk/report/local-government-in-scotland-financial-overview-201920>

Date 15 February 2021

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3 Background/Main Body of Report

Each year the Accounts Commission produces an overview of issues that have arisen from their local authority audits. In line with the previous publications these will again be encompassed in two reports. The first report, which is covered in this paper, focuses on financial performance of Councils and IJBs during 2019/20, and the other, Local government in Scotland: Challenges and performance which is expected to be published in May 2021, will highlight issues that the Commission, through its strategy, has identified as being of greatest importance, including the current and future challenges councils are facing, pressures on key services, how councils have responded to budgetary pressures and changing demand on services, and councils' performance and progress in meeting challenges.

Local government in Scotland: Financial Overview 2019/20 was published by the Accounts Commission in January 2021. The overview report of the 2019/20 financial year, provides a high-level independent, public assessment of how effectively Scottish local government is managing public money and responding to the financial challenges it faces. It is aimed primarily at councillors and senior council officers as a source of information and to support them in their complex and demanding roles. It is in four parts:

- Part 1: Councils' Income in 2019/20
- Part 2: Councils' Financial Position in 2019/20
- Part 3: Councils' Financial Outlook
- Part 4: Integration Joint Boards' Overview 2019/20

In her introduction the Chair of the Accounts Commission highlights the vital role that Councils and Integration Joint Boards (IJBs) have in supporting Scotland's communities. This has been amplified by the Covid-19 global pandemic. Covid-19 has fundamentally affected local government services and increased the uncertainty of how those services will be provided in the future. The financial impact of the pandemic on our public services is extreme. At the same time, we have seen the strength and resilience of many communities highlighted as they have worked with public service partners to provide invaluable support to those who need it most.

The report noted that in 2019/20, before the pandemic really took hold in Scotland, the financial impact of Covid-19 was limited and that more councils added to their usable revenue reserves than in previous years. Reserves play an important role in effective financial management and provide a cushion for future unexpected events. The emergence of the global pandemic and resultant UK lockdown from 23 March 2020 could be described as a once-in-a-lifetime event and Council reserves can be a key tool to manage the medium-term financial impacts of Covid-19.

The report further noted that Scottish Government funding accounts for the majority of council income. After several years of reductions in funding, there has been a real terms increase in 2019/20. It is important to note though that around 40 per cent of the increase was intended to meet the Scottish Government's policy of expanding early learning and childcare provision. As we have reported before, councils have limited flexibility over how they use this type of additional funding. It is also important to recognise that although funding in 2019/20 improved, reductions in local government funding over the past six years are still larger than in other areas of the Scottish Government budget.

Capital funding had experienced significant increases in the past three years by 33 per cent between 2017/18 to 2019/20. But Scottish Government capital funding in 2020/21 is now decreasing by 30 per cent in real terms. This will have an impact on councils' future investment plans.

In IJBs, the bodies set-up to deliver local health and social care services, the financial pressures are significant, with many needing additional funding from councils and health board partners to break-even in 2019/20. We also continue to see a high turnover in leadership in many IJBs, at a time when they are tackling both the impact of Covid-19 along with the ongoing and longer-term pressures of increased demand.

2020 presented significant challenges to the preparation and audit of councils', pension funds' and IJBs' annual accounts. However, 92 per cent of annual accounts were signed off by the revised audit deadlines due to the dedication of local government finance staff and of our auditors in these challenging circumstances. I am grateful for everyone's hard work and diligence to achieve this outcome.

During 2020/21, the pandemic and associated lockdown has affected many aspects of Councils' and IJB's finances and created significant financial uncertainty. Councils face the challenge of meeting additional mobilisation and recovery costs as well as the lost income resulting from closures of leisure facilities and reductions in income from fees and charges. Councils are also administering support schemes on behalf of the Scottish Government. Substantial additional funding for councils has been announced by the Scottish Government together with some further financial flexibilities, but it is currently unclear whether this will cover all cost pressures faced by councils in 2020/21 and beyond.

2020/21 also saw a large shift in the way that public services and communities worked together to support those most in need. Many communities and individuals stepped in to provide much needed local services and were empowered and encouraged to do so by councils, IJBs and their partners.

We have heard of much good practice and hope that this continues.

The Accounts Commission's future reporting, together with the Auditor General for Scotland, will be refocused on the significant impact of Covid-19 across all public services. This report highlights the emerging and developing financial challenges due to Covid-19, but future financial overview reports will be better able to assess the full year impact in 2020/21, based on financial reporting to 31 March 2021. The Local Government Overview 2021 report, due to publish in May, will consider the initial response phase of the pandemic.

4 Key Messages

The key messages identified in the 2019/20 report include:

- Councils' funding and income increased by £0.8 billion in 2019/20. There was an increase in Scottish Government funding of £0.5 billion, but reductions over the past seven years are still larger than in other areas of the Scottish Government budget.
- Nearly half of the increase in Scottish Government funding in 2019/20, and all the initial additional funding in 2020/21, was to fund the expansion in early learning and childcare.
- Councils continue to plan for, and deliver, savings as part of their annual budgets, but there are significant variations in individual councils' ability to deliver planned savings.
- More councils added to their usable revenue reserves totalling £65 million (net) in 2019/20.
- Glasgow City Council's equal pay funding strategy had a significant impact on total reserves, debt and capital expenditure this year (2019/20).
- The financial cost of Covid-19 on councils in 2020/21 is estimated to be £767 million, with just over half due to lost income. We estimate that funding announced by November 2020 meets 60 to 70 per cent of the cost pressures identified by councils, although total costs and funding are still uncertain
- Councils' auditors reported wider medium-term financial implications of Covid-19.
- A majority of IJBs (22) struggled to achieve break-even in 2019/20 and many received year-end funding from partners.
- Total mobilisation costs for Health and Social Care Partnerships for 2020/21 due to Covid-19 are estimated as £422 million. It is not yet clear whether the Scottish Government is to fund all of these costs.
- Instability of leadership continues to be a challenge for IJBs. There were changes in chief officer at 12 IJB's in 2019/20.

5 Financial Overview 2019/20

Part 1 - Councils' Income in 2019/20

- Councils' funding and income increased by £0.8 billion in 2019/20.
- The cash increase in Scottish Government funding (£0.5 billion) in 2019/20 improved the position relative to others, but reductions over the past seven years are still larger than in other areas of the Scottish Government budget.
- Nearly half of the increase in Scottish Government funding in 2019/20 was to fund the expansion in early learning and childcare.

The position with income will be familiar to Elected Members from their experience in developing the Medium Term Financial Strategy and setting annual budgets.

Part 2 – Councils' Financial Position in 2019/20

- On the whole councils continue to deliver savings as part of their budget in 2019/20, but there are significant variations in individual councils.
- In 2019/20 councils' auditors reported wider medium-term financial implications of Covid-19.
- More councils added to their usable revenue reserves in the year totalling £65 million (net).
- Two councils are at risk of running out of general fund reserves in the medium-term if current trends continue.
- Glasgow City Council's equal pay funding strategy had a significant impact on total reserves, debt and capital expenditure this year.
- Councils had the highest level of capital expenditure of the last five years.
- Local auditors drew attention to material uncertainty in property and investment valuations due to Covid-19
- Local government pension funds returns were negatively affected by Covid-19, but the majority of funds still tended to outperform their benchmarks.

Again the key messages reflect the challenges the Council faces. The real terms reduction in the value of resources available to the Council reinforces the importance of the Council's Medium Term Financial

Strategy which sets out the plans which ensure the sustainability of services and the increasing importance of maintaining robust financial management and reporting. In that regard Committee will also recollect from the Annual Auditors report that the Council achieved a green rating for Financial Management, and reflecting the external factors, an Amber rating for Financial Sustainability.

All councils hold an uncommitted general fund to protect against unforeseen financial pressures. Exhibit 7 in the report sets out Council's General Fund reserves as a proportion of net annual revenue split between committed, uncommitted and HRA. The exhibit provides a useful comparison of Midlothian's uncommitted General Fund position compared to other councils.

Council has a significant requirement to invest in assets to support the growing population. Though the level of borrowing is increasing the Treasury Management Strategy and prudential indicators provide Council with reassurance that this level of investment is financially sustainable and can be serviced from the revenue budget.

There is no doubt that difficult decisions lie ahead for all councils and the report highlights the importance of being proactive in addressing the financial pressures.

Part 3 – Councils' Financial Outlook

- 2020/21 initial budgets identified savings targets as the main way to close a budget gap of £0.5 billion, with more councils setting multi-year indicative budgets.
- Before the impact of Covid-19, Scottish Government revenue funding in 2020/21 increased by 1.4 per cent in real terms, but this is to fund the expansion in Early Learning and Childcare.
- The financial cost of Covid-19 on councils in 2020/21 is estimated to be £767 million, with just over half due to lost income.
- We estimate that funding announced by the Scottish Government by November 2020 meets 60 to 70 per cent of the cost pressures identified by councils through COSLA's cost-gathering exercise, although total costs and funding are still uncertain.
- Scottish Government capital funding to local government in 2020/21 is decreasing by 30 per cent in real terms.
- Councils need to review and revise their medium-term financial plans due to Covid-19.

The approval of the Medium Term Financial Strategy in June 2019 was an important step-change and one that provided greater certainty for local communities and also for employees. It has allowed the Council to

shift from having to consider savings each and every year at February Council meetings to planning for the medium term and in turn securing continued financial sustainability.

As a result the approval of the Medium Term Financial Strategy and, on the recommendation of the Business Transformation Steering Group, the subsequent approval of the 2020/21 budget ensured that the Council secured a strategic budget which invested in Midlothian to help it fulfil its potential to be a great place to grow.

The Medium Term Financial Strategy has provided a strong foundation on which the Council has been able to build its response to the financial impact of the Covid pandemic. A pandemic which continues to bring unprecedented financial challenges, risks and uncertainties for Local Government during the current financial year, for the 2021/22 budget, and which will likely impact on Council budgets for a number of years to come.

It is against this backdrop that a corporate solution was developed to support the achievement of balanced budgets for 2021/22 and 2022/23, the two budgets which will be required to be determined during the remaining term of this Council.

On 23 February 2021 Council set a budget for financial year 2021/22 which did not include any additional service reductions.

Part 4 – Integration Joint Boards' Overview 2019/20

- A majority of IJBs (22 of 30) struggled to achieve break-even in 2019/20 or recorded deficits.
- Total mobilisation costs for Health and Social Care Partnerships for 2020/21 are estimated as £422 million. It is not yet clear whether the Scottish Government is to fund all these costs.
- Revisions will be required to medium-term financial plans to reflect the impact of Covid-19.
- There were changes in chief officer at 12 IJBs in 2019/20.

The Midlothian IJB has continued to deliver delegated services within the resources allocated to it by both the Council and NHS Lothian. Like all IJB's Midlothian continues to face significant financial challenges given the increasing demand for services.

It is expected that the overview report will also be presented to the Midlothian IJB Audit and Risk Committee.

6 Report Implications (Resource, Digital, Risk and Equalities)

6.1 Resource

There are no additional resource implications.

6.2 Digital

There are no IT issues arising from this report at this time.

6.3 Risk

There are no additional direct risks associated with this report.

6.4 Ensuring Equalities

This report does not recommend any change to policy or practice and therefore does not require an Equalities Impact Assessment.

6.5 Additional Report Implications (See Appendix A)

Appendices

Appendix A – Additional Report Implications

Appendix B – Background Information/Links

APPENDIX A – Additional Report Implications

A.1 Key Priorities within the Single Midlothian Plan

Midlothian Council and its Community Planning Partners have made a commitment to treat the following areas as key priorities under the Single Midlothian Plan:-

- Reducing the gap in learning outcomes
- Reducing the gap in health outcomes
- Reducing the gap in economic circumstances

This report does not directly impact Midlothian Council's key priorities but a key message within the Accounts Commission report is that the way Council's respond to the financial challenge will inevitably impact on how they can deliver of key priorities and outcomes.

A.2 Key Drivers for Change

Key drivers addressed in this report:

- ☐ Holistic Working
- ☐ Hub and Spoke
- ☐ Modern
- ☐ Sustainable
- ☐ Transformational
- ☐ Preventative
- ☐ Asset-based
- ☐ Continuous Improvement
- ☐ One size fits one
- ☒ None of the above

A.3 Key Delivery Streams

Key delivery streams addressed in this report:

- ☐ One Council Working with you, for you
- ☐ Preventative and Sustainable
- ☐ Efficient and Modern
- ☐ Innovative and Ambitious

A.4 Delivering Best Value

The report does not directly impact on Delivering Best Value.

A.5 Involving Communities and Other Stakeholders

This report does not directly relate to involving communities and stakeholders.

A.6 Impact on Performance and Outcomes

The report does not directly impact Midlothian Council's and wider partners performance and outcomes but it does stress the need to

ensure consideration is given to the wider strategic planning and objectives as part of the council's response to the findings noted in the report.

A.7 Adopting a Preventative Approach

This report does not directly impact actions and plans in place to adopt a preventative approach.

A.8 Supporting Sustainable Development

The recommendations in this report support Midlothian Council's position in relation to delivering sustainable services going forward.

APPENDIX B**Background Papers/Resource Links (if applicable)**

Accounts Commission - Local government in Scotland: Financial Overview 2019/20 – (January 2021).