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## NORTH AYRSHIRE COUNCIL

### Agenda Item

13 February 2019

North Ayrshire Council

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**Title:** **Audit Scotland Report: Local Government in Scotland: Financial overview 2017/18**

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**Purpose:** To inform Council of the findings of the recent Audit Scotland report.

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**Recommendation:** That Council (i) notes the findings of the recent Audit Scotland report, (ii) notes the current position in North Ayrshire and (iii) considers these as part of the budget deliberations

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#### 1. Executive Summary

1.1 Audit Scotland published its 2017/18 financial overview of local government in Scotland at the end of November 2018. The timing of the report is intended to give councils the opportunity to use its findings to inform their budget setting. A link to the report is attached below;

[Audit Scotland Report: Local Government in Scotland Financial Overview 2017/18](#)

1.2 The report provides a high level independent analysis of the financial performance of councils during 2017/18 and their year-end financial position. It also comments on the financial outlook for councils. The report has a summary of key findings with more detail provided in four parts covering;

- Councils' budgets and spending in 2017/18;
- Councils' financial position;
- Integration Joint Boards' overview 2017/18; and
- Councils' financial outlook.

1.4 The report sets out a number of questions that councillors may wish to consider to help them understand their council's financial position and scrutinise its financial performance. These questions are published in a separate supplement. A link to the document is attached here;

[Local Government Financial Overview 2017/18: Scrutiny Tool for Councillors](#)

1.5 Appendix 1 to this report highlights the key messages identified within the Audit Scotland report and notes the current position of North Ayrshire Council in relation to these.

1.6 A copy of the Actions emerging from the 2017/18 Audit is attached at Appendix 2.

## **2. Background**

### **Financial Overview 2017/18**

2.1 The report examines the strategic financial position of local government in Scotland in 2017/18.

2.2 A summary is provided within the report with further information provided in 4 main sections:

- Part 1 - Councils' budgets and spending in 2017/18;
- Part 2 - Councils' financial position
- Part 3 - Integration Joint Boards' overview 2017/18; and
- Part 4 - Councils' financial outlook.

### **2.3 Key Messages**

#### **Audit Scotland Report**

2.3.1 Common themes emerge across the Summary and the 4 Parts of the report, some of which have been contained within previous Audit Scotland overview reports. These are summarised below;

- councils dependency on Scottish Government funding and the continuing significant financial challenges, with funding not keeping pace with increasing costs, demands and new policy commitments and in particular the impact of this on non-protected services;
- the protection of education and social work being met from reductions in other services;
- councils managing their funding gaps through savings and use of reserves;
- the need for councils to identify risk and develop contingency plans around EU withdrawal;
- the high level of debt of some councils relative to their size and the strategies to fund this;
- high level commentary on a number of issues relating to IJBs including; growth in funding, financial sustainability, reserves and medium term financial planning;
- publication of the Scottish Government five year financial strategy and the potential impact of this on local government funding levels;

- Councils progress on medium and long term financial planning and early stage delivery of transformational change.

### **North Ayrshire Council**

2.3.2 An update on the North Ayrshire position is noted below;

- the Long Term Financial Outlook approved at Council on 4 October 2017 is the cornerstone of the Council's financial planning framework and outlines the scale of the potential financial challenge facing North Ayrshire Council by 2027/28;
- the council continues to review its 3 year rolling medium term financial plan as part of the annual budget setting;
- Having delivered savings of £92m over the period 2010/11 to 2018/19 identification of new options is becoming increasingly challenging;
- Similar to the national position education and health and social care have been protected relative to other services;
- Transformation 2 has been closed off and next phase transformation will be incorporated into the new Council Plan;
- Council's unearmarked reserves are sitting at the minimum acceptable level of 2% with a bi annual review of all reserves undertaken;
- Reserves have supported non-recurring investment and the core budget since 2017/18;
- the council borrows for capital investment in line with its approved capital plan with affordability confirmed in its Treasury Management and Investment Strategy;
- need to ensure robust financial discipline across services continues to be applied;
- continued financial support for the Health and Social Care Partnership to deliver outcomes within the agreed financial envelope and repay the £5.8m debt to the Council;
- regular reporting to Audit and Scrutiny on the risks and mitigation of Brexit

2.3.3 All actions identified as part of the Council's external audit, as referenced at Appendix 2, have been progressed.

## **3. Proposals**

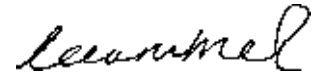
3.1 That Council notes the findings of the recent Audit Scotland report and the current position in North Ayrshire.

#### 4. Implications

<p><b>Financial:</b></p>	<p>The Audit Scotland report highlights the reliance of local government on Scottish Government grant funding and the need for the development of robust medium and longer term financial plans to develop sustainable solutions to bridge the anticipated funding gap.</p> <p>North Ayrshire Council develops medium term financial plans on a three year rolling basis and Council approved the (10 year) Long Term Financial Outlook on 4 October 2017. Financial sustainability, including the need to ensure an appropriate level of reserves, is a focus of the annual external audit.</p> <p>The challenging position of IJBs is noted, whilst this is a matter for IJBs it is important to the Council as a key funding partner.</p>
<p><b>Human Resources:</b></p>	<p>As part of a sustainable financial strategy the Council continues to actively manage the size of its workforce. Regular communication and consultation takes place with the workforce and Trade Unions.</p>
<p><b>Legal:</b></p>	<p>There are no direct legal implications associated with this report.</p>
<p><b>Equality:</b></p> <p><b>Children and Young People;</b></p>	<p>Equality impact assessment are carried out for all options identified as part of the medium and long term financial plans</p>
<p><b>Environmental &amp; Sustainability:</b></p>	<p>There are no direct environmental and sustainability implications associated with this report.</p>
<p><b>Key Priorities:</b></p>	<p>In addressing the financial challenges which it faces, the Council seeks to minimise the impact on delivering its key priorities.</p>
<p><b>Community Benefits:</b></p>	<p>There are no direct community benefits associated with this report.</p>

**5. Consultation**

5.1 There was no requirement to consult on the preparation of this report.



LAURA FRIEL  
Executive Director (Finance and Corporate Support)

**Reference:**

For further information please contact Laura Friel, Executive Director  
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**Background Papers**

None

## Audit Scotland: Local Government in Scotland Financial Overview 2017/18

### Summary

Ref	Key Message	NAC Feedback
<b>S1</b>	Councils depend on Scottish Government funding for a significant part of their income. Scottish Government revenue funding to councils reduced in 2017/18, in cash terms by 0.6 per cent (£0.06 billion) and in real terms, by 2.3 per cent (£0.22 billion). Council tax increases and increased fees and charges were used by councils to increase overall budgets by £0.3 billion (cash terms).	The initial core grant settlement to North Ayrshire Council in 2017/18 reduced by £9.2m (3.44%). This was augmented by £3.484m of non-recurring funding as the Scottish Government (SG) Budget progressed through the Parliamentary process, amending the final reduction to 2.14%. This funding was later confirmed as recurring as part of the 2018/19 SG Budget. Additional ring fenced funding of £4.340m was provided for the new Pupil Equity Fund. The 3% uplift in council tax alongside additional income from the Council tax band changes and other less significant changes provided £4.614m of additional funding. Additional income from Increased fees and charges was £0.090m.
<b>S2</b>	In 2017/18, councils managed funding gaps of four per cent in their net expenditure budgets of £12 billion, mainly through savings and planned use of reserves. Councils are under pressure to find different ways to fund and deliver services. In 2017/18, 24 councils increased council tax, whereas in 2018/19, all councils increased council tax.	In 2017/18 the North Ayrshire budget gap as a result of less funding and additional cost of service delivery, including recognised pressures, was £7.139m representing 2.2% of the recurring funding base. Non-recurring funding of £8.782m was applied in 2017/18 to support non-recurring investment and the establishment of a challenge fund to support transformation in the health and social care partnership. In recognition of the pressures on local government funding North Ayrshire has increased council tax in each of the years following the lift of the freeze and has complied with the Scottish Government cap of 3%.
<b>S3</b>	Overall increases in spending in Education and Social Work were offset by reductions in other services.	In 2017/18 73% of the savings came from Economy and Communities and Place which represent 23% of the council's total budget. This position continued into 2018/19 but to a lesser extent with 38% of the savings being delivered by Economy and Communities and Place, this reducing contribution reflects the level of savings which these services have delivered since 2010/11.

Ref	Key Message	NAC Feedback
S4	Eighteen councils ended 2017/18 with lower levels of usable reserves than they had at the start of the year. Total usable reserves fell by £18 million, a relatively small amount.	<p>The level of useable reserves for North Ayrshire at the end of 2017/18 was broadly similar to that at the start of the financial year. Reserves are reviewed twice per annum, when closing the Accounts and setting the Budget to ensure they reflect future commitments and the risk profile of the Council.</p> <p>The Council used £8.782m of reserves to fund services in 2017/18 and £3.500m in 2018/19.</p>
S5	Funding to the Integration Joint Boards (IJBs) increased in 2017/18 by three per cent in cash terms (1.4 per cent in real terms), including additional funding from the NHS. The majority of IJBs have underlying financial sustainability issues, with 20 incurring deficits or dependent on additional ('deficit') funding from their partners.	<p>In 2017/18 NAC increased its funding to the North Ayrshire IJB (NAIJB) by £2.985m, an increase of 3.4%. The NA IJB hasn't delivered in year financial balance since inception with the Council providing additional funding in the shadow and initial year. As a result of additional funding not being provided since 2016/17 the NA IJB has a deficit of £5.8m, with the debt being owed to the Council. Plans are in place for these funds to be repaid, commencing in 2018/19. Establishment of a discrete Chief Finance and Transformation Officer and more robust financial planning and management is helping the HSCP progress towards financially sustainable service delivery in 2018/19.</p>
S6	The financial outlook is for reductions in Scottish Government revenue funding to councils. This will mean continued and increasing financial pressures on council services, especially those that are not protected	<p>North Ayrshire Council has delivered savings of £92m between 2010/11 and 2018/19 meaning that future reductions will be more challenging. The Council's transformation programme alongside a different relationship with our communities will seek to mitigate the impact of future savings.</p> <p>As noted at S3 it is becoming increasingly difficult to deliver savings from the non-protected elements of the Council's budget.</p>
S7	The impact of EU withdrawal is not yet clear, but councils need to identify the risks and develop contingency plans to manage these risks	<p>The Audit and Scrutiny Committee of North Ayrshire Council receives regular updates on risks and mitigation associated with Brexit. The Council participates in a number of national bodies to ensure it is fully informed of emerging risk to allow it to assess further mitigations.</p>

## **Part 1 Councils' budgets and spending in 2017/18**

<b>Ref</b>	<b>Key Message</b>	<b>NAC Feedback</b>
<b>P1 (1)</b>	Councils depend on Scottish Government funding for a significant part of their income. Scottish Government revenue funding to councils reduced by 2.3 per cent (£0.2 billion) in real terms in 2017/18, but council tax, grants to services and fees and charges increased, and overall budgets grew by £0.3 billion in cash terms.	Almost 85% of NAC's funding is from Scottish Government Grant.  Refer to S1
<b>P1 (2)</b>	Between 2013/14 and 2017/18, funding from the Scottish Government to local government decreased at a faster rate, 6.92 per cent, than the Scottish Government revenue budget at 1.65 per cent.	Between 2013/14 and 2017/18 the reduction to North Ayrshire Council's core budget was £12.307m, 5.2%. Alongside this additional funding of £15.780m was provided to support new Scottish Government policies.
<b>P1 (3)</b>	Distribution of funding from the Scottish Government is based mainly on population but could be more transparent to ensure clarity about how funding distribution reflects factors that drive demand and costs in councils.	North Ayrshire would support a review of the current funding and distribution formula to ensure total resources support core services alongside new policy priorities and ensure appropriate cognisance is taken of deprivation.
<b>P1 (4)</b>	In 2017/18, councils managed funding gaps of four per cent in their net expenditure budgets of £12 billion, mainly through savings and planned use of reserves. Their outturn at the year-end was better than budgeted.	Refer to S2 and S4.  The Final outturn for North Ayrshire in 2017/18 was a breakeven position after earmarking £2.5m to support the 2018/19 financial plan.
<b>P1 (5)</b>	Overall increases in spending in Education and Social Work were offset by reductions in other services	Refer to S3

## **Part 2 Councils financial position**

<b>Ref</b>	<b>Key Messages</b>	<b>NAC position</b>
<b>P2 (1)</b>	Eighteen councils drew on their usable reserves in 2017/18, overall by a relatively small amount.	Refer to S4
<b>P2 (2)</b>	Some councils have relatively higher levels of debt for their size.	North Ayrshire Council borrows in line with its long term capital investment programme and treasury management and investment strategy. The Council's annual loan charges are 5%



Ref	Key Messages	NAC position
		of the net General Fund expenditure, with overall affordability set out in the Treasury Management and Investment Strategy.
<b>P2 (3)</b>	Local policies vary on whether cash and investments are held to support reserves. This could increase the need for further future borrowing.	<p>North Ayrshire's treasury management function ensures that the Council's funds are managed in accordance with the relevant professional codes, such that sufficient cash is available to meet service activity. This involves organisation of the cash flow and where capital plans require, appropriate borrowing.</p> <p>In line with the above and in the interests of best value the Council continues to be "under borrowed" by £50.5m, as at 31 March 2018, this means that the Council is using internal funds to support its capital financing requirements.</p>
<b>P2 (4)</b>	Capital expenditure in 2017/18 decreased by five per cent in real terms. Housing and education were the main areas of investment. Despite this the number of social houses provided by councils continues to fall.	<p>North Ayrshire's General Services' final General Fund capital expenditure for 2017/18 was £32.0m compared to £48.7m in 2016/17. The 2016/17 expenditure included £24.5m expenditure on major capital projects at Garnock Campus and Irvine Leisure Centre.</p> <p>North Ayrshire has an ambitious programme of investing in its existing housing stock and plans to build 803 new house by 2023. In 2017/18 £25.5m was capital investment was made in the Council's housing stock, alongside £17.2m of revenue investment. As at 31 March 2018 271 new houses have been built as part of the Council's 1,375 ten year target.</p>
<b>P2 (5)</b>	Some councils have had significant increases in their debt positions.	<p>Refer to P2(2) and P2(3)</p> <p>In 2017/18 North Ayrshire borrowed in line with its long term capital investment programme and treasury management strategy. The level of borrowing was £27.1m more than 2016/17, primarily due to a new DBFM arrangement, £45.4m, partly offset by reduced short term borrowing, £18.3m.</p>
<b>P2 (6)</b>	There were delays with the valuation of pension's liabilities in councils across Scotland in 2017/18, but the net pension liability has reduced substantially in 2017/18.	The Council is reliant on the Strathclyde Pension Fund to provide timely accurate information on the net position of the Fund. A revaluation of the net position required some late adjustments to the Council's Unaudited Accounts.
<b>P2 (7)</b>	Management commentaries in councils' accounts should do	A significant review of the format and content of the Council's

Ref	Key Messages	NAC position
	more to explain financial outturn against budget.	Management Commentary was carried out in 2018/19. The Council's external auditors recognised this as an example of best practice.

### **Part 3 Integration Joint Boards' overview 2017/18**

Ref	Key Messages	NAC position
<b>P3 (1)</b>	Funding to the IJBs increased in 2017/18 by three per cent in cash terms. Most of this additional funding came from the NHS and includes additional Scottish Government funding to the NHS for IJBs of £107 million.	Refer to S5.  The information noted at S5 reflects the additional funds made available by the Council for the IJB. The North Ayrshire share of the additional £107m made available via the Health Settlement was £3.1m. This funding was earmarked to meet the additional costs of living wage in purchased social care and sleepovers.
<b>P3 (2)</b>	The majority of IJBs have underlying financial sustainability issues, with 11 out of 30 incurring deficits in 2017/18. A further eight would have incurred deficits without additional ('deficit') funding from their partners.	Refer to S5.
<b>P3 (3)</b>	Reserve positions vary enormously between IJBs.	Refer to S5  The North Ayrshire IJB has a Reserves Policy. Financial performance to date has prevented the IJB from building up reserves.
<b>P3 (4)</b>	Medium-term financial planning is not used by most IJBs and further improvements to financial management should be introduced.	The North Ayrshire IJB's medium term financial plan was approved in March 2017, this is being refreshed currently with a revised plan being presented to the IJB in March 2019. A number of concerns had been raised about financial management with the HSCP with a report being presented to the IJB Performance and Audit Committee and the Council's Audit and Scrutiny Committee. Steps have been taken to improve performance with the November 2018 financial performance report showing a significant improvement in delivering services within the approved budget.

#### **Part 4 Councils' financial outlook**

<b>Ref</b>	<b>Key Messages</b>	<b>NAC position</b>
<b>P4 (1)</b>	In 2018/19, Scottish Government revenue funding to local government increased by 0.2 per cent after two years of real-terms reductions.	<p>The core grant settlement for North Ayrshire Council was a marginal increase of £0.136m, 0.05%. Similar to 2017/18 additional funds had been made available to local government as the SG Bill progressed through Parliament.</p> <p>In addition to the core Settlement £6.266m was made available to fund Scottish Government policy, including community justice, health and social care and ELC expansion.</p>
<b>P4 (2)</b>	The Scottish Government published a five-year financial strategy in May 2018, but multi-year budgets are not yet being developed. The financial strategy identifies greater future uncertainty and likely further reductions of nine per cent in real terms over the next five years in 'other non-protected' council funding.	The Scottish Government five year financial strategy summarized the key national policies. Allocation of funding aligned to the policy will continue to be through the Scottish Government Budget. The Strategy sets out the anticipated less favourable funding position of non-protected services, the most significant of which is local government. A movement towards multiyear Financial Settlements is essential to provide greater certainty and support more effective medium and longer term financial planning.
<b>P4 (3)</b>	Many councils are in the early stages of delivering transformational change.	A summary report on delivery of T2, the Council's current transformation programme will be presented to Cabinet on 12 February 2019. This demonstrates that 23% of savings over the period of the plan were delivered through transformation. The Council Plan which is due to be considered by Council on 17 March 2019 sets out the next phase transformation aligned to the new Plan, this will evolve as new transformation initiatives are identified.
<b>P4 (4)</b>	Medium-term financial planning has been adopted by almost all councils,	The Council considers a rolling three year Medium

Ref	Key Messages	NAC position
	but less than half have significant long-term plans over five years.	Term Financial Plan when it sets its annual budget. This is underpinned by the Long Term Financial Outlook which was approved by Council in October 2017.
<b>P4 (5)</b>	Councils expect to manage smaller funding gaps in 2018/19 of £0.3 billion (two per cent), with all 32 councils raising council tax rates by three per cent in 2018/19. There are no councils where the budgeted use of reserves is a critical issue over the next three years.	North Ayrshire was required to deliver savings of £10.482m (3.2%) in 2018/19, after applying reserves of £3.5m and increasing council tax by 3%. This compared with £7.140m in 2017/18.
<b>P4 (6)</b>	The impact of EU withdrawal is not yet clear, but councils need to identify the risks and develop contingency plans to manage these risks, as far as possible.	Refer to s7

# Action plan

## Recommendations for improvement

Area	Recommendation	Management response	Responsible person	Target date	Priority
Transformation programme	The Council acknowledge that at present it currently doesn't have a clear plan to demonstrate how its transformational activity across the Council will achieve the required financial benefits to address the significant funding gap over the medium to longer term. We recommend that this is progressed to ensure that the Council can clearly demonstrate how services plan to change to meet the challenging financial position. It is important that there is clear member input into the process, with effective collaboration between members in order for the transformation of service delivery to be successful.	A refreshed transformation plan will go to the Transformation Board and to Cabinet later in 2018/19 and will incorporate progress against the T2 programme including savings delivered to date, key transformation themes and projects, engagement and governance arrangements.	Chief Executive	31 March 2019	High
Cash reconciliations	In the absence of a functioning automatic cash reconciliation process within the new ledger system, the Council should implement a manual reconciliation process to allow period end cash balances to be fully reconciled in a timely manner (see page 16).	A manual reconciliation process has been implemented for all cash balances and the Council continues to work with the software provider to develop the functionality of the automated process.	Head of Finance	31 March 2019	High

# Action plan (continued)

## Recommendations for improvement (continued)

Area	Recommendation	Management response	Responsible person	Target date	Priority
Reporting to Members	The process involved in reporting to Cabinet should be reviewed to determine if reporting can be performed in a more timely manner. Currently, reporting to Cabinet on each period typically takes place two months after period end (see page 33).	Outwith Cabinet reporting regular engagement takes place with Services. An immediate review of the Cabinet reporting timetable for 18-19 indicates a 6 week timeframe from period end until Cabinet reporting, with the exception of the first report due to summer recess. Financial reporting to Cabinet includes a detailed forecast position to the financial year end as opposed to variance analysis up to the reporting period. Arrangements will be kept under review to try and secure earlier reporting.	Executive Director of Finance and Corporate Support	31 March 2019	Medium
Non Domestic Rates grant	Management should ensure that all required reports and information be pulled from the NDR system as at year end for the purpose of the external audit (see page 16).	The Non Domestic Rates year end procedures will be revised to ensure that all required information is available.	Head of Finance	31 March 2019	Low