



James Dornan MSP
Convener, Local Government and Communities Committee

By email: LocalGovernmentandCommunities@parliament.scot

3 March 2021

Dear James

We are writing to the Local Government and Communities Committee by way of follow up to the questioning and discussion on Council reserves on 10 February. COSLA, SOLACE and Directors of Finance (DoF) believe it is important to articulate the position in relation to reserves in more detail, and to describe the situation for this year in particular, given the impact of the pandemic.

Local Government is unique in a Public Sector context in having the legal power to hold reserves. This gives councils greater flexibility to manage funds across the financial year end, allows funds to be set aside to manage financial risks and enables investment in efficiency programmes. Based on local circumstances, these reserves are committed or “ear-marked” for a variety of purposes (including policy commitments, transformation programmes to meet future demand, equal pay, key infrastructure projects, and severe winter weather). This reflects that Councils are autonomous and are not provided with funding from the Scottish Government when they face financial hardship. This can be contrasted to NHS Boards who receive support from the Scottish Government via brokerage when they experience financial difficulties. Councils therefore require a level of reserves to manage the risks they face and for the DoF to discharge their statutory duty to ensure that Councils operate within available resources and remain financially sound over the short, medium and long term.

Discussions at the Committee centred on the implication that reserves should be used this year to meet budget pressures associated with pandemic. Councils are adopting a variety of strategies this year to balance books, including use of reserves, but to deplete these would not be prudent, nor would it allow councils to enable recovery over the medium term.

Committee members quoted figures from [Audit Scotland’s 2019-20 Financial Overview](#), in which usable reserves of £2.6bn were reported (£2bn revenue; £0.6bn capital).

However, in this context, it is only appropriate to look at **revenue** reserves, which totalled £2bn in 2019-20 (based on unaudited accounts). Only £1.3bn (64%) of this total reserve is General Fund. Other elements within the total are Housing Revenue Account (HRA) Balance £188m (9%), Renewals & Repair Fund £139m (7%), Insurance Fund £101m (5%) and Other £335m (15%). In terms of a council’s ability to address one-off investments and financial “shocks” such as legal claims, it would only be the General

Fund reserves that could be used, as it would not be appropriate, for example, to use reserves committed for Insurance Fund, and HRA balances.

Even within the General Fund reserves, there are well established and important commitments – for example in Fife, there are £13.6m of commitments already against the General Fund reserve of £32.7m, including commitments for affordable housing from Council Tax generated from second homes, ear marked carry forwards and funding for transformation initiatives. This means that of the “headline” figure of £69.77m reported by Audit Scotland for Fife, only £19m is usable to meet budgetary pressure (or **27%** of the total reserves reported). This scenario will be replicated across other councils, albeit there will be variation across the country (for good reason including reserves held to deal with severe winter weather).

If the Audit Scotland figures for 2019-20 are examine further, there is a total of £345m of “unearmarked” revenue reserves. Local Government Finance circular [4/2020](#) shows that for 2019-20, revised Total Estimated Expenditure was £12,394m. This means that 2.8% is being held in reserve - previous Audit Scotland guidance has suggested between 2 and 4% is prudent. However, the level of reserves required will vary depending on the financial exposure and risk that a Council faces. The pandemic has significantly increased the financial risk that Councils face, and each Director of Finance will take a view on the level of reserves required over the medium term. A higher level of reserves is likely to be required given the current financial exposure.

It is also important that reserves are not used to fund recurring expenditure as this would become unsustainable. The use of reserves in this manner would store up problems to be addressed in future years rather than identifying recurring solutions to balance budgets on an ongoing basis, and something that Audit Scotland does not view favourably.

As we approach the year end, there are a number of Ministerial announcements that have resulted in additional funding for Local Government in 2020-21, and instances where Scottish Government policy teams have approached COSLA to look at alternatives to the award of a specific grant, including grants that were intended for 2021-22. This means that significant sums will now be awarded as general revenue funding and paid as a redetermination in March 2021. This utilises the unique powers that Local Government has and ensures that Scottish Government does not breach its own carry forward restrictions. There is a similar scenario in relation the health funding, with funding being passed to Health and Social Care Partnerships late in the financial year, which will have to be held in reserves by councils.

Whilst this funding approach, and the flexibilities it offers, is now to be welcomed, it has created considerable work for both Scottish Government and Councils during 2020-21 (award and acceptance of grants, claims, reporting etc) and will add to reserves, albeit they will be earmarked for specific policy purposes.

As the Committee is aware, COSLA and Directors of Finance have been working with Scottish Government to secure a range of fiscal flexibilities that can be used to alleviate budget pressures. Use of the flexibilities may also see Council reserves increase in this and next financial year. However, the impacts of COVID will require to be addressed by Councils for some time to come and flexibility will be required to address wide ranging

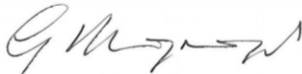
issues beyond the immediate pressures identified to date, and over the medium to long term. Accessing these flexibilities, once all are agreed, would allow Councils to support important activity that is aligned to national priorities such as addressing poverty, supporting economic recovery and building back communities.

In summary:

- reported total usable reserves do not reflect what is actually available for use to alleviate budget pressures caused by COVID;
- for the reasons described above, and for the ultimate benefit of our communities, council reserves will increase during 2020-21, but will be critical for dealing with the ongoing impacts of the pandemic.

Should you require any more information at this stage, please do not hesitate to contact Sarah Watters- Chief officer Local Government Finance, sarah@cosla.gov.uk

Yours truly,



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