

# Finance and Resources Committee

10am, Thursday, 7 March

## Principles of the Local Government Finance Settlement

Item number	7.1
Executive/routine	
Wards	n/a
Council Commitments	n/a

### 1. Recommendations

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- 1.1 Members of the Committee are asked to:
  - 1.1.1 note the contents of the report;
  - 1.1.2 refer the report to the Governance, Risk and Best Value Committee for its information and scrutiny; and
  - 1.1.3 note that further updates will be provided to both Committees as the joint review between COSLA and the Scottish Government in this area progresses.

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## Principles of the Local Government Finance Settlement

### 2. Executive Summary

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- 2.1 Following an earlier request from members of the Governance, Risk and Best Value Committee, the report provides an overview of the process by which council-specific revenue grant funding allocations are determined as part of the Local Government Finance Settlement.

### 3. Background

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- 3.1 At the meeting of the Governance, Risk and Best Value Committee on 15 January 2019, members considered the Accounts Commission's *Local Government in Scotland Financial Overview* for 2017/18. The overview report includes, in Paragraphs 13 to 20, a number of observations on the current process by which available funding is distributed amongst Scotland's thirty-two councils. The overview report concludes that it is important for COSLA and the Scottish Government to assure themselves that the funding formula developed to fulfil this aim remains fit for purpose.
- 3.2 In considering this overview report, members of the Governance, Risk and Best Value Committee asked that a report setting out the basis of current funding allocations, and the work being carried out by COSLA and the Scottish Government to review current arrangements, be brought to the Finance and Resources Committee and referred thereafter to the Governance, Risk and Best Value Committee for scrutiny. Following agreement by members of the Finance and Resources Committee, this report addresses this request.

### 4. Main report

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- 4.1 The process for determining the quantum of funding available to local authorities in Scotland has evolved significantly in recent years in line with wider constitutional changes. The introduction of the fiscal framework between the UK and Scottish Governments, facilitating progressive devolution of Income Tax-related powers to the Scottish Parliament, has introduced greater flexibility, but also greater potential volatility, in the overall level of resourcing available to the Scottish Government. The quantum of grant funding then made available to Local Government is, in turn, influenced by both the Scottish Government's relative policy priorities and other

revenue-raising powers made available to councils. This latter aspect now includes not only Council Tax and other statutory and discretionary fees and charges but, following the Cabinet Secretary's announcement of the revised Local Government Finance Settlement for 2019/20, the potential availability of a number of new revenue-raising powers, most notably transient visitor and workplace parking levies, in appropriate circumstances.

### **Role of the fiscal framework**

- 4.2 The fiscal framework was jointly agreed between the Scottish and UK Governments to allow the Scottish Government to manage the powers contained within the Scotland Act 2016 whilst ensuring broad alignment to arrangements in the rest of the UK. A key feature of the Act is the progressive devolution of rates and bands of Income Tax, resulting in the creation, from April 2016, of the Scottish Rate of Income Tax.
- 4.3 The devolution of income tax-raising powers forms part of the wider financial empowerment of the Scottish Parliament. This progressive devolution of powers is summarised in Appendix 1. Once the full powers contained within the 2016 Act have been transferred, almost half of the total resources available to the Scottish Government will fall, albeit to varying extents, within its control.
- 4.4 Despite this empowerment, the level of block grant received from the UK Treasury remains the largest single determinant of the overall level of resource available to the Scottish Government. Based on spend on public services in England, the Scottish Government is automatically allocated a population-based share of changes in spending on public services devolved to Scotland through the workings of the Barnett Formula, resulting in an updated block grant. From this block grant are made adjustments for projected retained revenues from Income Tax, Land and Buildings Transaction Tax and Scottish Landfill Tax (as shown in Appendix 2). Other things being equal, positive variation from equivalent income projections for the rest of the UK will result, in overall terms, in the availability of additional resources relative to the levels had they remained under the control of the UK Government and vice-versa.

### **Local Government Finance Settlement (LGFS)**

- 4.5 While councils in Scotland raise over £1 billion annually through levying statutory and discretionary fees and charges for the services they provide, the majority of their funding is received through a combination of General Revenue Grant (GRG), retained Non-Domestic Rates (NDR) income and Council Tax.

### **Client group approach**

- 4.6 The Settlement is based on the "client group" approach, an evidence-based method seeking to quantify different authorities' relative need to spend on particular services. This assessment is grounded upon identifying the main determinant of spending need for a particular service (based on those in actual, or potential, receipt of the service concerned, such as local authority pupil numbers for school

education or those aged 65 or over for older people's social care), termed the primary indicator, tempered by other agreed factors demonstrating a statistically-significant relationship with actual expenditure (secondary indicators). These secondary indicators also reflect the fact that the unit cost of meeting service demand may be higher in some areas. The unit cost of providing school-based services in a rural setting, for example, may be higher due to smaller class sizes (with greater relative numbers of teachers) or higher transportation costs. A more deprived local authority area may also experience greater calls on some demand-led services (such as debt advice) and/or receive lower income from charges (such as leisure services), influencing the net cost of provision.

### **Grant-Aided Expenditure**

- 4.7 By undertaking this analysis across the full range of services provided by local government, when converted to a monetary value based on the overall Scotland-wide assumed spending requirement, this gives each authority a GAE (Grant-Aided Expenditure) assessment. Wherever possible, these GAE calculations are updated on an annual basis to take account of the most currently-available data.
- 4.8 Appendix 3 ranks the various primary and secondary indicators according to the amount of the total GAE allocated with reference to each for the actual 2018/19 Settlement. From this analysis it can be seen that population numbers, whether at an aggregate level or across specific age cohorts (including school pupil numbers) are a key determinant, although measures of rurality and deprivation are also influential. While the extent to which deprivation is recognised within the funding formula is supported by regularly-updated statistical analysis, this, along with the appropriateness of "freezing" GAE quantum at 2007/08 levels and any wider need to re-assess current allocation bases given evolving policy intentions at national level, will likely form part of the joint Scottish Government and COSLA review.
- 4.9 As each authority's total GAE takes into account an assessment of its relative spending need compared to that of other councils, this should theoretically allow a uniform level of service to be provided (and the same level of Council Tax to be levied) irrespective of an authority's population, location or relative deprivation. It is nonetheless important to emphasise that GAE allocations are neither budgets nor grant funding as such; they are merely used to inform the grant support allocation process and councils are not required to allocate their overall funding accordingly. The key factor in the LGFS is, however, how a council's *relative* share of the overall assessed need compares to that of other councils. This is particularly important at a time of real-terms reductions in available resources when the level of per capita funding per unit of "need" is reducing.
- 4.10 To an authority's total assessed expenditure requirement is then applied a series of further adjustments. These items include amounts provided in respect of formerly-ringfenced grants, revenue support for historic borrowing and the application of the "floor" stability mechanism.

### **Floor stability mechanism**

- 4.11 The effect of the floor mechanism is to guarantee a minimum year-on-year level of increase in grant (or, in recent years, a maximum level of decrease) to each council, with this level determined with reference to the average for all councils. This adjustment is intended to provide a greater degree of stability to authorities whose assessed spending need would otherwise see their level of grant increase by less (or decrease by more) than this. The flipside of this safety mechanism is that those authorities whose change in grant is better than this minimum level contribute in proportion to their overall level of grant. In this way, the mechanism is self-financing and thus requires no additional Scottish Government funding in overall terms. Members of the Committee will be aware that the Council has received significant support from the floor in recent years, with its level of GRG increased by over £13m in 2019/20.

### **85% funding “floor”**

- 4.12 Although also referred to as a funding “floor”, the Scottish Government introduced for the first time in 2012/13 a separate mechanism under which each authority is provided with per capita funding equal to at least 85% of the Scottish average. Members are reminded that the 85% floor is about absolute levels of, rather than year-on-year changes in, grant funding. Edinburgh received significant support in the initial years of this policy but, following the updating of population estimates to take full account of the 2011 census results, this funding reduced and was then lost entirely in 2017/18. Following incorporation of updated population estimates, the Council will, however, again receive £1.7m in additional funding in 2019/20 in respect of this calculation and will be the only council to benefit.

### **Non-Domestic Rates income**

- 4.13 Since 2011/12, all NDR income raised in a council area has been retained within it, meaning that there is no redistribution of resources across Scotland as was the case in previous years. It is important to stress, however, that a corresponding adjustment has been made to general revenue grant, such that combined grant and business rates income is unaffected (as the underlying assessment of need has not changed).

### **Determination of General Revenue Grant funding**

- 4.14 The grant funding calculation then makes an assumption about the level of income councils can raise based on a notional Council Tax level and the estimated number of Band D equivalent properties within the authority, adjusted for reliefs and exemptions. This sum is deducted from the overall assessed funding requirement, adjusted for any ring-fenced grants, to derive the combined amount of revenue grant funding and retained business rates income to be provided to each council as follows:

## **Overall need to spend (as assessed by Scottish Government)**

less assessed level of Council Tax income available to authority

less ring-fenced grants

less Non-Domestic Rates income collected by the authority

= General Revenue Grant

## **5. Next Steps**

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- 5.1 As part of the revised Local Government Finance Settlement announced on 31 January 2019, the Cabinet Secretary for Finance, Fair Work and Economy confirmed that work would shortly begin to develop a rules-based framework for local government funding in partnership with COSLA, to be introduced for the next Parliament. This framework is expected to be developed along similar lines as the existing fiscal framework between the Scottish and UK Governments. Members of the Committee will be kept apprised of this work as it progresses.
- 5.2 In recent years, COSLA has placed particular emphasis upon the need for future sustainability of funding arrangements for local government, with the quantum of funding for core services key in this context. It has, however, also made the case for greater fiscal empowerment for local government through an ability, in appropriate circumstances, to levy discretionary taxes. The Scottish Government's recent announcements, as part of the revised LGFS announcement on 31 January, on both the transient visitor levy and workplace parking levy have the potential to contribute positively to this empowerment of democratic and financial accountability.
- 5.3 Following the earlier recommendations of the Scottish Budget Review Group, the Scottish Government has also indicated that it will bring forward a three-year funding settlement for local government from 2020/21 onwards.
- 5.4 At a more operational level, a subgroup of the Settlement and Distribution Group, comprising section 95 Chief Financial Officers from a number of Scotland's councils, worked closely with Scottish Government colleagues to review the operation of the stability funding floor, as well as potential means of consolidating or reducing the number of existing separate funding allocations with a view to increasing the transparency of the current distribution process. A number of these changes were reflected in the 2019/20 Settlement process.

## **6. Financial impact**

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- 6.1 There is no direct additional impact of the report's contents but it sets out a number of considerations impacting upon the current level of grant funding received.

## **7. Stakeholder/Community Impact**

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- 7.1 There is no direct additional impact of the report's contents.

## **8. Background reading/external references**

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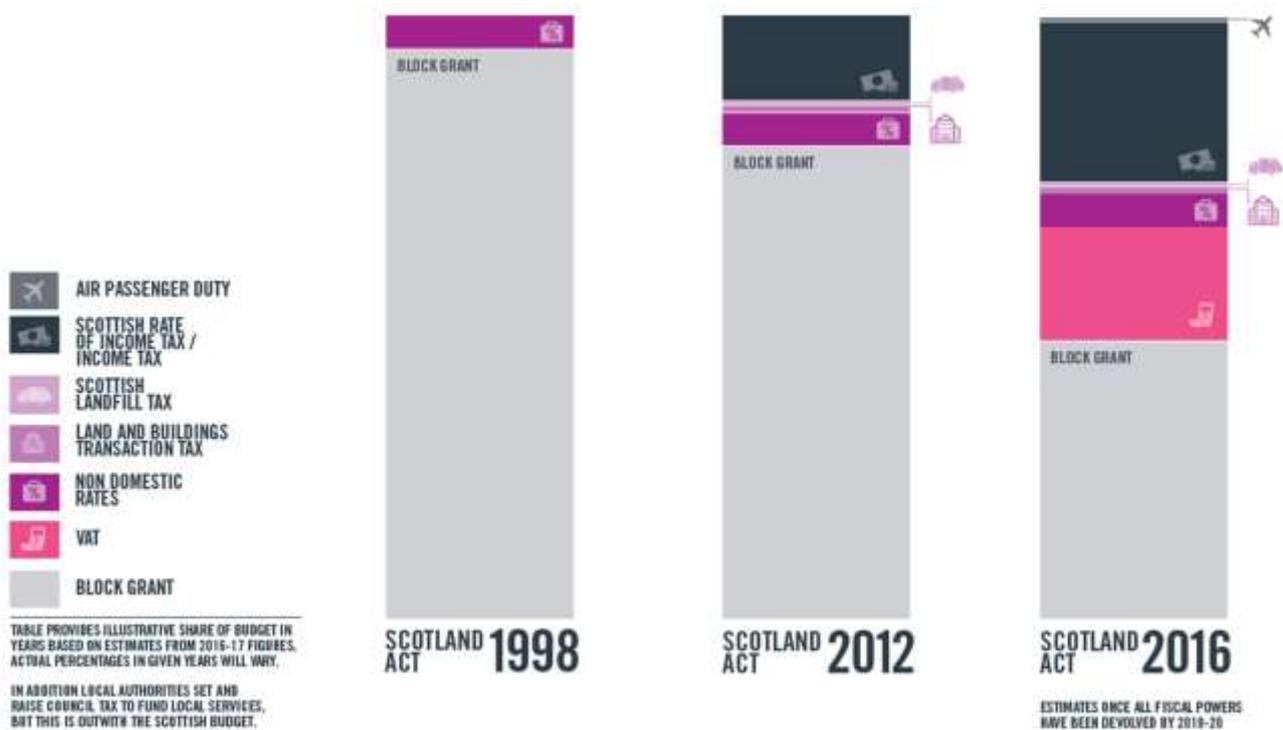
- 8.1 [Local Government in Scotland: Financial Overview 2017/18](#), Accounts Commission, November 2018

## **9. Appendices**

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- 9.1 Appendix One - Progressive devolution of income-raising powers under Scotland Act 2016
- 9.2 Appendix Two - Interaction of UK and Scottish Government budgets through fiscal framework
- 9.3 Appendix Three - Determinants of overall GAE assessment

## Appendix 1 – Progressive devolution of income-raising powers under Scotland Act 2016



Under the Scotland Act 1998, the Scottish Parliament had control of less than 10% of devolved expenditure in Scotland. Assuming planned assignment of VAT revenues is implemented as part of the Scotland Act 2016, almost 50% of tax revenues will be controlled by the Scottish Parliament.

In contrast, the majority of welfare benefits and policies remain reserved to the UK Government, with only 15% of Social Security spend currently controlled by the Scottish Parliament.

## Appendix 2 – Interaction of UK and Scottish Government budgets through fiscal framework



The Scottish block grant continues to be calculated by the Barnett formula, but an adjustment needs to be made to reflect that some of the budget is now funded by Scottish tax revenues that were previously retained by the UK Government. There are two steps to the adjustment:

- (i) an initial block grant deduction is made for each tax. This is to compensate the UK Government for the tax revenue which is now being retained by the Scottish Government. These adjustments ensure that the UK and Scottish Governments are no better or worse off as a direct result of devolution; and
- (ii) for each subsequent year the block grant adjustments (BGAs) for each tax are grown or "indexed" to take account of changing tax revenue over time.

## Importance of Indicators within the GAE Settlement

### Primary Indicators - Distributional Effect

Indicator	Grant Aided Expenditure	
	£000s	Share (%)
<b>All Pupil Primary Indicators</b>	<b>3,026,151</b>	<b>38.31%</b>
<b>All Population Primary Indicators</b>	<b>1,848,955</b>	<b>23.41%</b>
Secondary Sector Pupils	1,141,745	14.45%
All School Pupils	907,192	11.48%
Primary Sector Pupils	902,523	11.42%
Residential Accommodation for the Elderly Composite Indicator	562,900	7.13%
Services for Home Base Elderly Composite Indicator	550,079	6.96%
Population Aged 16-64	432,555	5.48%
Total Population	340,244	4.31%
Community & Residential Care for Children Composite Indicator	327,681	4.15%
Total Education GAE (excluding NPAF and FEF)	315,428	3.99%
Weighted Road Lane Length	296,908	3.76%
Population Aged 2-19	243,588	3.08%
Adjusted Population (Parks & Remainder of Leisure)	188,462	2.39%
Adjusted Population (Waste Disposal & Eviro Health)	180,351	2.28%
Pre-School Provision for 4 Year Olds	155,177	1.96%
Total Dwellings	131,105	1.66%
Adjusted Population (Sports Facilities & Swimming Pools)	85,839	1.09%
Adjusted Population (Libraries)	85,412	1.08%
Pupils Taking Meals	74,691	0.95%
Adjusted Population (Street Cleaning)	69,022	0.87%
Urban Lane Length	68,474	0.87%
Weighted Free School Meals Registration	59,005	0.75%
Population Aged 5-15	54,853	0.69%
Population Aged Under 5	54,141	0.69%
Selected Social Work GAEs for General Administration	51,899	0.66%
Population Aged 3&4	26,215	0.33%
Population Aged 60+	24,722	0.31%
Non-Domestic Rateable Subjects	22,461	0.28%
Population Aged 0-14	21,225	0.27%
Population Aged 0-3	18,920	0.24%
Homeless & Threatened with Homelessness Applications	16,579	0.21%
Area of Maintained Burial Ground	13,009	0.16%
Population Living in Settlements of less than 1,000	9,591	0.12%
Number of Ethnic Minority Pupils	8,317	0.11%
Number of Education Establishments	7,587	0.10%
Population Aged 3&4 Living in Settlements of less than 1,000	7,518	0.10%
Minimum Payments	7,383	0.09%
Number of Current Income Deprived	4,278	0.05%
Population (excl those living in national parks)	3,980	0.05%
Length of Off-Road Paths (excl national parks)	3,980	0.05%
Building Control Warrants	3,833	0.05%
Population Aged 17+	2,317	0.03%
Weighted Aids & HIV+ Cases	1,729	0.02%
Cremations in Local Authority Owned Crematoria	417	0.01%
SG Department Allocations	203,145	2.57%
Previous Settlement Shares Rolled Forward	17,168	0.22%
<b>TOTAL</b>	<b>7,703,648</b>	<b>97.52%</b>

## Importance of Indicators within the GAE Settlement

### Secondary Indicators - Redistributive Effect

INDICATOR	GAE Redistributed by Indicator (% of total GAE)
Percentage of Pupils in Small Rural Schools	0.37%
Island Local Authority Adjustment	0.04%
Population Dispersion	0.14%
Income Support Dependants per 1,000 Aged 0-19	0.06%
Urban Settlement Pattern	0.10%
Hostel Places per 1,000 Pupils	0.10%
No of Body Type - Car Licences per Km Unweighted Lane Length	0.67%
Road Density/Area Deprivation	0.08%
Rural Settlement Pattern	0.04%
<b>TOTAL</b>	<b>1.61%</b>

### Secondary Indicators - Redistributive Effect by Individual Assessment

Service	Secondary Indicator	Amount Redistributed (£000)	Amount Redistributed
Primary School Teaching Staff	Percentage of Pupils in Small Rural Schools	29,228	3.24%
Secondary School Teaching Staff	Island Local Authority Adjustment	3,185	0.28%
School Transport	Population Dispersion	9,132	16.65%
School Meals	Income Support / JSA Dependants per 1,000 Aged 0-19	3,038	4.07%
School Hostels & Clothing	Hostel Places per 1,000 Pupils	8,085	29.95%
School Hostels & Clothing	Income Support / JSA Dependants per 1,000 Aged 0-19	1,839	6.81%
Road Maintenance	No of Body Type - Car Licences per Km Unweighted Lane Length	46,040	23.58%
Winter Maintenance	No of Body Type - Car Licences per Km Unweighted Lane Length	6,908	10.64%
Parks & Open Spaces	Urban Settlement Pattern	7,234	5.60%
Waste Collection	Population Dispersion	2,303	2.80%
Street Cleaning	Road Density/Area Deprivation	6,280	9.10%
Environmental Health	Rural Settlement Pattern	1,289	1.89%
Consumer Protection	Rural Settlement Pattern	1,705	9.51%
School Crossing Patrols	Urban Settlement Pattern	975	7.46%
<b>TOTAL</b>		<b>127,239</b>	

**Budget Based, Actual Expenditure and Share of Specific Grant Based GAEs**

Indicator	Grant Aided Expenditure	
	£000s	Share (%)
Gaelic	5,570	0.07%
Residual FE Travel & Bursaries	5,492	0.07%
Ferries	13,027	0.16%
Airports, Harbours	3,035	0.04%
Glasgow Underground - Share of SPTA Population	8,668	0.11%
Tourism	12,374	0.16%
Museums & Art Galleries	29,786	0.38%
Planning & Economic Development	90,728	1.15%
Non-Road Lighting	7,461	0.09%
Supported Employment	8,350	0.11%
Admin of Housing Improvement Grants & Loans	4,493	0.06%
Trading Services	1,384	0.02%
Coast Protection	758	0.01%
Flood Prevention	4,891	0.06%
<b>TOTAL</b>	<b>196,017</b>	<b>2.48%</b>
<b>GAE TOTAL</b>	<b>7,899,665</b>	<b>100.00%</b>