Local government in Scotland

Financial bulletin 2023/24

ACCOUNTS COMMISSION

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Contents

Accessibility

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Key facts

Some of these are based on a sample – see paragraph 4 for further information on our methodology

Funding and budgets

- **1.8 per cent:** the real-terms reduction in revenue funding from the Scottish Government in 2023/24 compared to 2022/23
- **21 per cent:** the proportion of Scottish Government revenue funding that was ring-fenced or directed towards national policy commitments in 2023/24
- **£759 million:** the budget gap identified by our sample of 29 councils at the start of 2023/24. The 2024/25 budget gap identified by all 32 councils was £585 million
- **1.2 per cent:** the real-terms reduction in capital funding from the Scottish Government in 2023/24 compared to 2022/23.

Financial performance

- **3.3 per cent:** the real-terms reduction in councils' total revenue funding and income in 2023/24 compared to 2022/23
- **9 out of 29:** the number of councils that reported overspends against their agreed revenue budgets
- **11 out of 30:** the number of councils that achieved all their planned savings
- **25 out of 30:** the number of councils that reported lower expenditure than planned across their capital programmes in 2023/24
- **£19.8 billion:** councils' net debt in 2023/24, a 15.8 per cent increase on 2022/23, as councils become more reliant on borrowing to finance their capital programmes.

Financial position and outlook

- **5 per cent:** the decrease in councils' total usable reserves
- **84 per cent:** the proportion of the General Fund that is committed
- **12 out of 29:** the number of councils that made unplanned use of their reserves in 2023/24 to manage budget pressures
- **15 out of 30:** the number of councils that have long-term financial plans in place, with councils reporting difficulty planning for the longer term due to future uncertainty.

Key messages

Despite an increase in overall revenue and capital funding for councils in 2024/25, and the Scottish Government's budget proposals in December 2024 indicating a further real terms uplift in funding for 2025/26, the financial outlook for Scotland's councils remains challenging.

1. In 2023/24, councils' total revenue and income fell, including another real terms decrease in revenue funding from the Scottish Government. Councils are increasingly reliant on identifying savings, which becomes progressively more difficult year-on-year, and again used reserves to remain within their agreed budgets.

2. In 2023/24, capital funding remained constrained, with councils borrowing more and managing a range of complex funding models. Capital funding from the Scottish Government reduced slightly in real terms, continuing a longer-term trend. Capital expenditure was lower than planned. Councils continue to borrow more to enable investment in their estates and council debt, and annual interest costs, continue to increase.

3. In 2023/24, usable reserves, which are those that can be used to support service delivery, reduced and most are already committed for specific purposes. This presents an ongoing challenge for councils reliant on reserves to balance their budgets, as well as to longer-term financial sustainability. Using reserves to routinely balance budgets is not sustainable.

4 Councils need to intensify transformation activity, progressing at scale and pace to ensure their financial sustainability. How councils plan to use their reserves, make savings and transform their services needs to become more transparent. The need to consult local communities and clearly communicate the implications for local services of the budget decisions taken has never been more important.

Recommendations

In 2025, councils should:

- Report on the savings made within their management commentaries more comprehensively, including provision of comparisons to savings targets agreed during budget-setting, and whether they were recurring or non-recurring (paragraphs 29 - 30).
- Ensure that the impact of capital underspends, future borrowing projections and of using financial flexibilities on their indebtedness are reported clearly alongside the impact of these on future revenue budgets (paragraphs 34 - 41).
- Ensure reserves policies indicate explicitly and clearly the impact of financial flexibilities on reserves held; the nature, level of and intended timing of the deployment of committed usable reserves held; and the level of uncommitted and contingency funding held within General Funds (paragraph 54 and Case study).
- Prioritise service transformation, considering the impact of current service delivery models on longer-term financial sustainability, including the medium-term impact on reserve levels (paragraphs 61 - 62).
- Ensure that financial sustainability becomes a central focus of financial monitoring and reporting, making greater use of financial sustainability indicators within reports to elected members and within their regular public reporting and financial strategies and plans (paragraphs 63 - 67).

We note progress against the recommendations from our Financial bulletin 2022/23 in Appendix 1.

Introduction

About this report

1. This report is part of a series of overview outputs produced by the Accounts Commission which together provide an independent overview of the financial and operational performance of Scotland's local government sector.

2. This report examines councils' financial performance in 2023/24. This follows the unprecedented challenges of the Covid-19 pandemic and cost-of-living crisis and sits against a backdrop of the whole of the Scottish public sector facing challenges to its financial sustainability. The bulletin sets out:

- councils' funding and budget-setting
- councils' financial performance
- councils' position at the end of 2023/24 and the financial outlook.

3. In spring 2025, we will publish a budget briefing examining the 2025/26 budgets set by councils, including analysis of anticipated budget gaps and the decisions made by councils when setting their budgets. This will be followed by a report focused on service performance later in 2025.

Methodology

4. The primary sources of information for this report are councils' 2023/24 accounts and annual audit reports, a data request issued to councils in October 2024 and Scottish Budget documents.

5. Our findings are based primarily on:

- The 2023/24 annual accounts for 29 councils (20 audited and nine unaudited). At our 2 December 2024 deadline, accounts were unavailable for Clackmannanshire, Eilean Siar and East Dunbartonshire and these councils are not included in our 2023/24 analysis (or comparisons to previous years).
- Supplementary information from 30 councils collected via a data return issued to council directors of finance and was also reviewed by appointed auditors. At our 25 November 2024 deadline, data returns were unavailable for Clackmannanshire and Eilean Siar and these councils are not included in our analysis. We also utilised

elements of data returns previously submitted to us in support of our Financial bulletin 2022/23 report.

- Scottish Government Budget documents. Our analysis of Scottish Government funding reports on the funding position for all 32 of Scotland's councils.

6. When looking at trends, we convert some figures to real terms. This adjusts financial information from past and future years to prices for the year under review (ie, 2023/24). This is to take account of inflation so that trend information is comparable. To adjust for inflation, we use gross domestic product (GDP) deflators, which are published quarterly by HM Treasury. GDP deflators are the standard approach adopted by both the UK Government and Scottish Government when analysing public expenditure.

7. Financial trend data (both capital and revenue) relating to funding, income or expenditure will generally be shown in real terms. Financial information from the councils' accounts' balance sheets remains unadjusted. This includes trend analysis on reserves, sources of capital finance, borrowing and debt. These are not adjusted to real terms as they are already subject to revaluations within the councils' accounts to reflect current prices.

1. Council funding and budgets

Both revenue and capital funding from the Scottish Government to councils were reduced in real terms in 2023/24, with councils once again setting budgets that required significant gaps to be addressed.

Councils are reliant on Scottish Government funding which makes up over 60 per cent of income

8. As the largest source of funding or income for councils, at over 60 per cent, Scottish Government funding shapes the fiscal environment that councils operate in. Currently councils receive a single year settlement, with a draft allocation published in the Scottish Budget in December. This is revised throughout the year and in recent years a low initial settlement has been followed by large additional transfers during the financial year.

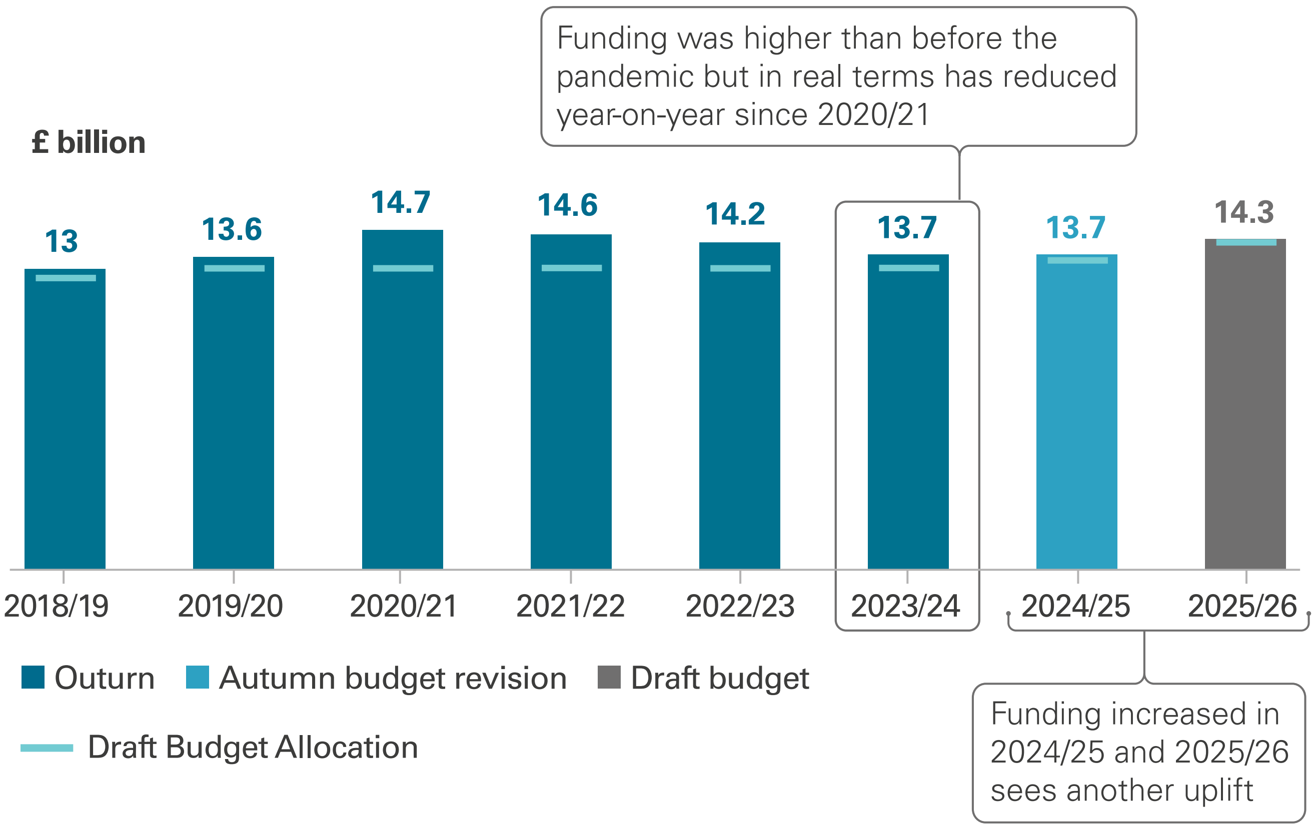
9. In 2023/24, the Scottish Government allocated councils total revenue and capital funding of £13.7 billion. This settlement was higher than before the pandemic but in real terms funding was reduced year-on-year since 2020/21. The 2024/25 settlement has reversed this trend and the 2025/26 draft settlement published in December 2024 indicates another real-terms uplift in funding for councils (Exhibit 1, page 10).

10. This initial 2025/26 draft settlement allocates £15 billion of revenue and capital funding to councils, a 5.8 per cent real terms increase on the 2024/25 draft settlement. Increases to revenue funding include an uplift to the general revenue grant, funding for pay awards and teachers' pensions. Increases to capital include additional funds to support inter-islands connectivity and climate change. There is still uncertainty as to how increased employers' National Insurance (NI) contributions, announced by the UK Government, will be funded. The Convention of Scottish Local Authorities (COSLA) estimates these will be an additional £265 million cost pressure for councils in 2025/26.

11. The funding increase for councils recently announced as part of the Scottish Government's 2025/26 draft budget in December 2024 does not change the fact that the financial outlook remains challenging (Part 3). We will examine the implications of the Scottish Budget for councils' own budget-setting in our next Local government in Scotland publication, Local government budgets 2025/26.

Exhibit 1.
Scottish Government revenue and capital funding to councils since 2018/19 in real terms

Funding in 2023/24 was higher than before the pandemic but in real terms has reduced year-on-year since 2020/21. This trend reversed in 2024/25 and 2025/26 sees a further funding uplift.



Note: Draft budget allocations include transfers from other portfolios. 2020/21 and 2021/22 totals include Covid-19 funding allocations. Barnett consequentials (and other funding) will be allocated to 2024/25 in the Spring Budget Revision. The draft 2025/26 settlement will be subject to additional in-year allocations that are already included in earlier year totals.

Source: Scottish Government Budget documents

Revenue funding from the Scottish Government fell by 1.8 per cent in real terms in 2023/24, despite significant in-year allocations

12. In 2023/24, revenue funding from the Scottish Government (at the spring revision) was £12.7 billion, a 4.2 per cent cash increase on the previous year but 1.8 per cent lower in real terms. General revenue grant funding and non-domestic rates combined decreased by 1.5 per cent. Specific revenue grants saw no cash increase which meant a reduction of 6.9 per cent in real terms.

13. Some further Scottish Government funding received by councils, although not formally ring-fenced, is provided with the expectation that it is directed to specific purposes. This is announced and distributed to councils in-year. In 2023/24, councils received an additional £1.6 billion at the autumn revision including additional funding to support teachers' salaries as well as the expected transfers from other portfolios including health and education. A further £0.3 billion was transferred from other portfolios at the spring revision.

14. In 2023/24, we calculated that ring-fenced and directed funding amounted to almost £2.7 billion, which is 21 per cent of Scottish Government revenue funding to councils. This is lower than in 2022/23. In the 2024/25 Scottish Budget, following a commitment in the Verity House Agreement to reduce the level of ring-fenced funding, a number of ring-fenced or directed items were 'baselined' into the general revenue grant. This includes all £522 million of the early learning and childcare specific revenue grant and £429 million of in-year transfers including adult social care Living Wage funding, Free Personal and Nursing Care and Free School Meals Intervention. While no longer ring-fenced, spending will still need to be directed towards these policies. In the 2025/26 Scottish Budget, initial indications do not show any significant alterations.

Councils identified £759 million of budget gaps at the start of 2023/24, and planned to use savings and reserves to address these

15. Councils set their own budgets in February and March for the financial year ahead using the initial allocation from the Scottish Government. At the time of setting their 2023/24 budgets, councils in our sample of 29 identified a cumulative **budget gap** of at least £759 million for the year. This represented a budget gap of 4.8 per cent of the total net cost of services.

During the budget-setting process, councils may identify a **budget gap**, which is the difference between their anticipated expenditure for the year and the funding and income they expect to receive. Councils will identify and agree bridging actions to allow them to set a balanced budget. This may include an agreement on savings to be made during the year.

16. To close the budget gap and set a balanced budget, councils took a range of actions. Over 90 per cent was covered by agreeing:

- to make £260 million of recurring savings (34 per cent of the total share)
- to make a further £30 million of non-recurring, one-off savings (four per cent)
- to use £202 million of reserves (26 per cent)
- to raise £144 million through increases to council tax (19 per cent)
- to use £73 million of funding released via application of financial flexibilities (nine per cent)[1] (Exhibit 2, page 13).

[1] The budget gap and values that make up the bridging actions vary from those published in last year's Financial bulletin as the sample is different and additional data returns were received post publication that are now included.

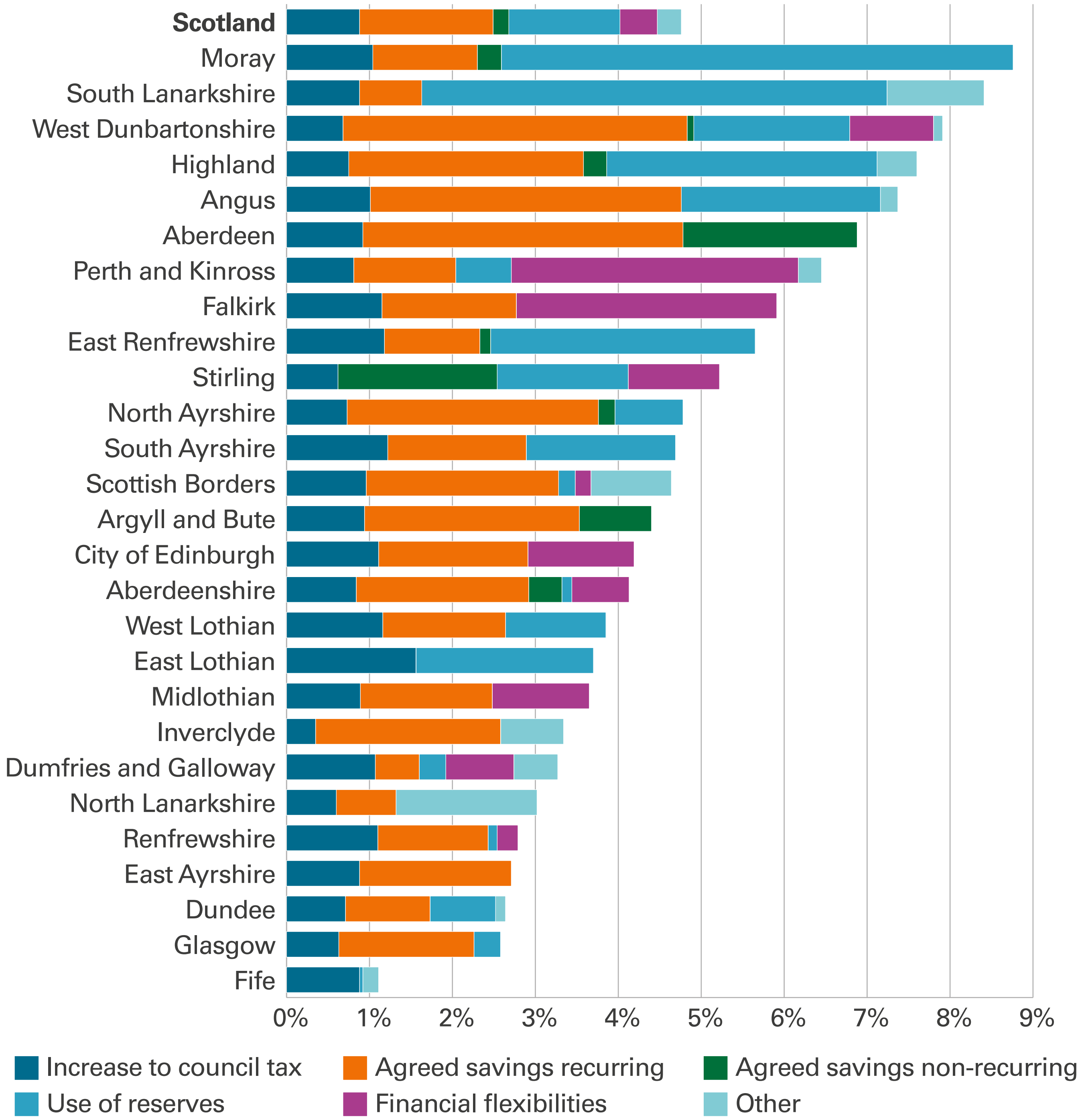
17. The use of reserves and other non-recurring measures is unsustainable and is only a temporary plug for a budget gap in that one year. The gap will remain in future years until recurring measures such as recurring savings or increases to income are found or the service cost base is reduced.

18. The setting of council tax levels is an important mechanism available to councils in delivering a balanced budget. In 2023/24, councils increased their tax by an average of 5.4 per cent. This was used to bridge 19 per cent of the overall budget gap. The Scottish Government imposed a council tax freeze for 2024/25, instead providing £144 million to 'fully fund' the freeze to the equivalent of a five per cent increase. The Cabinet Secretary for Finance and Local Government confirmed during her budget statement in December 2024 that there will be no council tax freeze or cap for 2025/26.

Exhibit 2.

The bridging actions councils identified within their 2023/24 budgets as a proportion of net cost of services

Recurring savings and using reserves made up the majority of how councils intended to meet their identified budget gaps.



Note: In addition to the three councils whose 2023/24 annual accounts were not available, Shetland and Orkney are excluded from this chart as both are outliers due to their high use of reserves to set their budget, reflecting the councils' regular utilisation of the returns from significant investments and harbour income. Shetland's bridging actions made up 35 per cent of their net cost of services (over 80 per cent of which related to reserves use). Orkney's bridging actions made up 13 per cent of their net cost of services (of which over 90 per cent was use of reserves).

Source: Council data returns (2023) and Councils' annual accounts 2023/24 (audited and unaudited)

With Scottish Government capital funding remaining constrained, councils are increasingly reliant upon borrowing to fund planned investment decisions

19. Capital funding from the Scottish Government (at the spring revision) fell by 1.2 per cent in real terms between 2022/23 and 2023/24 and was 21 per cent lower than 2018/19. Both the general capital grant and specific capital grant have decreased in real terms. The specific capital grant, the proportion of funding that is ring-fenced for specific uses, was much lower than five years ago and has been relatively static for the past three years. This is due to the completion of the capital element of the Early Learning and Childcare Expansion Programme. Councils received £70 million of capital funding for use in 2023/24, by allowing an equivalent amount of revenue reserves to be released, and a further £22 million of funding to support the cost of local government pay awards (for example by allowing councils to use this instead of planned transfers from revenue budgets).

20. Capital funding was reduced further in 2024/25. The initial draft allocation for 2025/26 saw an increase compared to 2024/25 but capital funding remains lower than 2023/24 and earlier years. The longer-term reduction in capital grants means councils are having to finance their chosen investment in new facilities by other means. Councils are now more reliant on other sources of finance, such as borrowing, transfers from their revenue budgets and making use of financial flexibilities, than has previously been the case (paragraphs 33 - 41).

2. Financial performance

Councils increasingly relied on savings and reserves to ensure they remained within agreed revenue budgets; capital expenditure was lower than planned and borrowing increased. Improvements in how councils report their savings are still needed.

Councils' total revenue funding and income fell by 3.3 per cent in real terms in 2023/24, with income from service fees still below pre-pandemic levels.

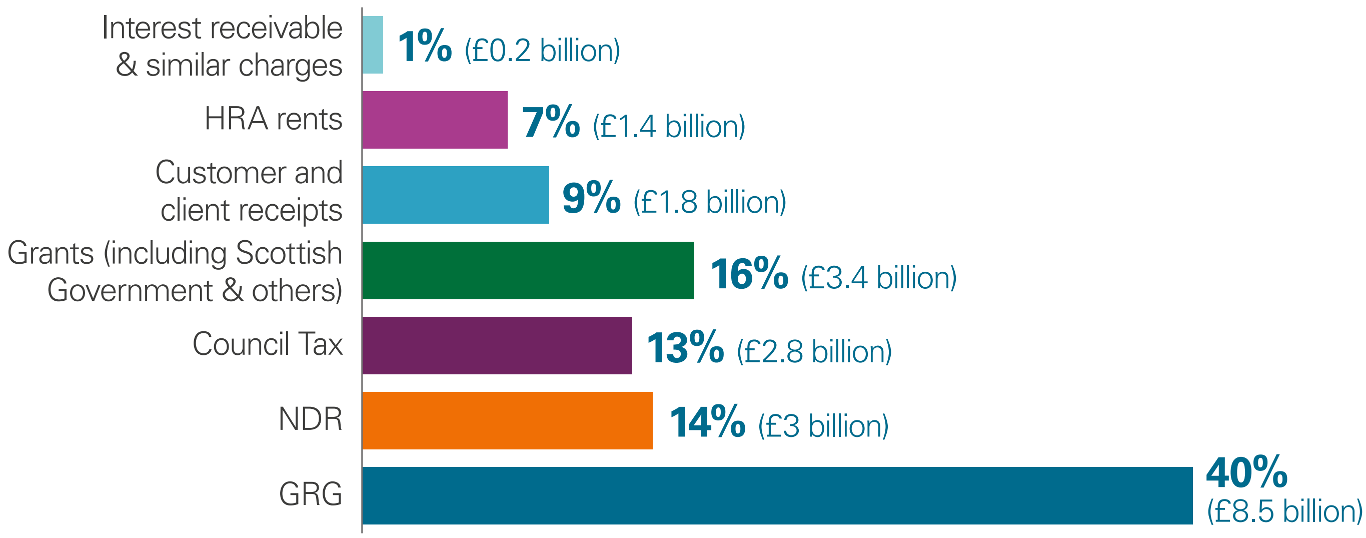
21. In addition to Scottish Government funding and council tax, councils receive funding and income from several other sources, including fees and charges for using services and council house rents (Exhibit 3).

22. In 2023/24, from our review of 29 councils' annual accounts, councils received £21.2 billion in revenue funding and income. This is £540 million more than 2022/23 but represents a real terms decrease of 3.3 per cent (£725 million) as increases in income have not kept pace with inflation. In 2023/24, total funding and income fell back to 2019/20 levels.

Exhibit 3.

Sources of council funding and income in 2023/24

The proportion of funding from each source is similar to 2022/23.



Note: Interest receivable refers to the interest that has been earned by investments, loans, or income to be received from overdue invoices.

Source: Councils' annual accounts 2023/24 (audited and unaudited) (based on 29 annual accounts)

23. Council tax is an important source of income for councils, providing £2.8 billion in 2023/24. The proportion has remained static for the last five years at around 13 per cent of total funding and income. In 2023/24, councils received £11 million more income from council tax than in 2022/23, which is a 0.4 per cent real terms increase.

24. Income from customer and client receipts dropped significantly during the pandemic and has not yet returned to previous levels. Customer and client receipts are 12 per cent (£253 million) lower in real terms than in 2019/20. Councils reported receiving lower income than budgeted for as a reason for service overspends in 2023/24 across a broad range of services, with parking and waste the most common. However, the picture is mixed and for some councils and service areas increased income offset expenditure and led to services underspending against their budgets. Income generation, and the limited capacity to increase this, was cited by a number of councils as a risk to financial sustainability.

Overall, councils remained within their agreed revenue budgets, but some services spent more than planned

25. In 2023/24, councils managed net budgets of around £15 billion, compared to £13.4 billion in 2022/23. Overall, councils reported a revenue budget underspend of £111 million or 0.7 per cent. This is around half the variance seen in 2022/23. Since 2019/20 there has been a small overall underspend each year and, except for 2020/21, this variance has decreased year-on-year. Despite the overall underspend, nine reported overspends against their agreed revenue budgets.

26. Councils reported both underspends and overspends at a service level, with workforce issues and income a common theme for both (Exhibit 4, page 17).

Exhibit 4.

Council overspends and underspends at a service level and reasons for them

Workforce issues and income generation are a common theme for both.

	Service area	Reasons for
Overspends	• Reported in a wide range of service areas with culture and leisure, children and families, education and adult social care being noted most often.	• Service area overspends were mostly attributed to a lack of funding, workforce pressures and general cost increases. • Underperformance of a range of income streams also contributed to overspends in some councils.
Underspends	• Education and early years were referred to most often. • Communities, culture and leisure, and planning and economic development were also identified by some councils as areas of underspend.	• Underspends in education and early years were often attributed to lower than anticipated demand and unfilled staff positions. • Underspends were sometimes attributed to more favourable income position, such as generating greater income than budgeted for and receiving additional VAT reimbursements. • Workforce issues, such as challenges with recruitment, and high vacancy levels, were also identified as a cause of underspends.

Note: Culture and leisure services were reported in both but twice as often as an area of overspend than an underspend.

Source: Council data returns

Councils delivered significant savings, but some remain reliant on one-off measures and reporting against savings targets should be more transparent

27. From our sample of 30, 28 councils set a savings target in 2023/24, totalling £362 million, with £332 million (92 per cent) being achieved. This is significantly higher than the savings target reported by the same councils last year (£214 million).

28. Of the 30 councils:

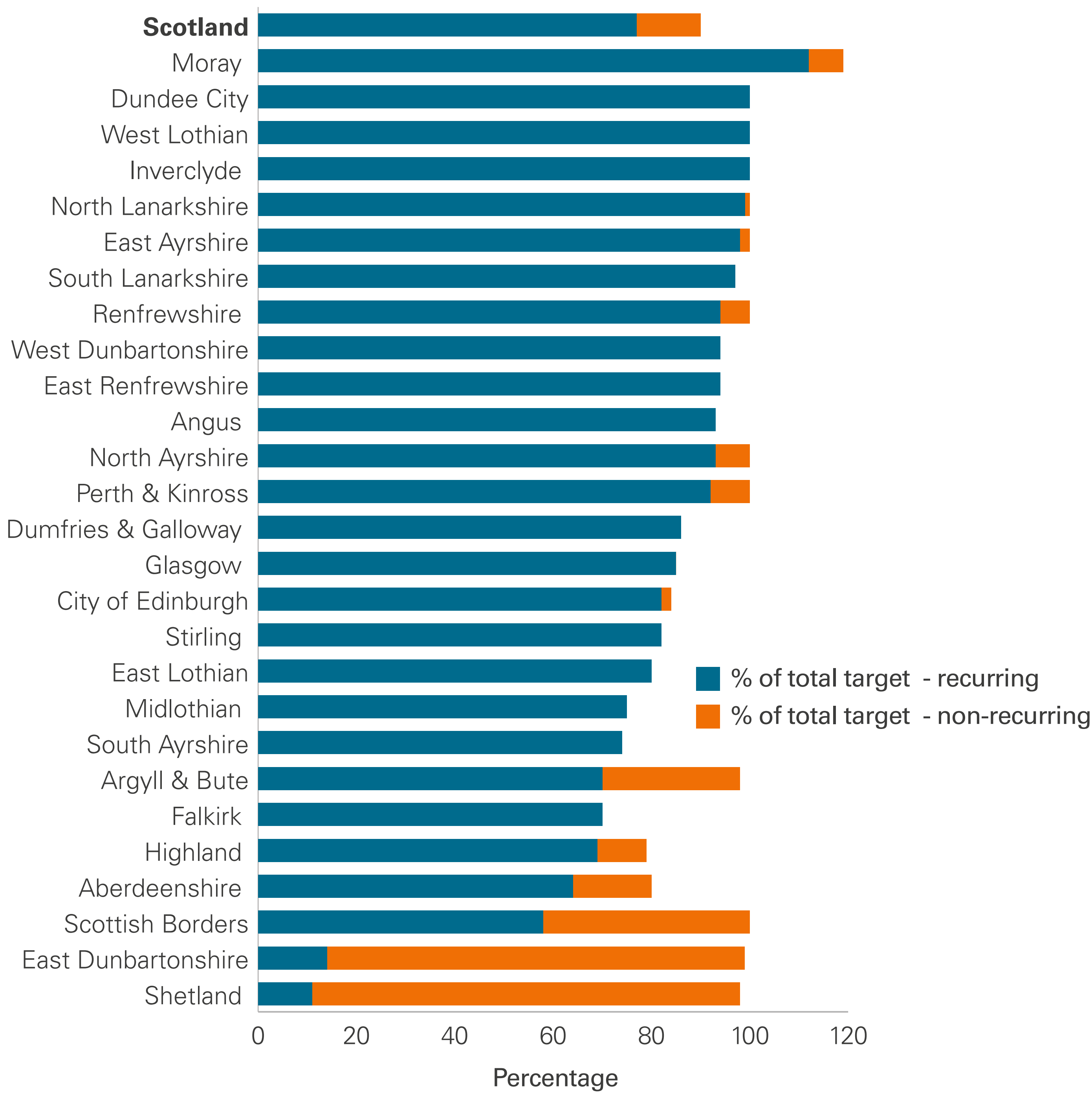
- eleven achieved their full savings target or more
- thirteen missed their target but achieved 80 per cent or more
- four achieved less than 80 per cent of their target
- two councils (Fife and Orkney) did not have savings targets in place.

29. Not all councils could split savings targets or achieved savings information into recurring or non-recurring categories. Where we have a breakdown of how savings were achieved (27), 85 per cent (£244 million) were achieved on a recurring basis, compared to 82 per cent in 2022/23. Non-recurring savings accounted for 15 per cent of total savings achieved, at £42 million (Exhibit 5, page 19).

Exhibit 5.

Proportion of savings targets achieved in 2023/24, split by recurring and non-recurring savings (based on 27 councils that can split their savings in this way)

Some councils continue to rely upon one-off measures to deliver in-year savings.



Note: In addition to the two councils that did not submit a data return, a further three councils are excluded from this exhibit. Aberdeen City sets a savings target to be achieved in the year but does not differentiate between recurring and non-recurring savings for monitoring purposes. The savings target was achieved for 2023/24. Fife and Orkney did not have a savings target in place in 2023/24.

Source: Council data returns

30. In our Financial bulletin 2022/23 we recommended that councils prioritise the achievement of recurring savings and avoid reliance on non-recurring measures. The overall extent of progress against our recommendation is difficult to assess due to a lack of detail and transparency in reporting on savings performance. Non-recurring savings are not always included in savings targets or performance information so it remains difficult to assess the overall reliance on these or, indeed, the overall savings achieved.

31. Additionally, a review of management commentaries within annual accounts found that not all councils are reporting progress against savings plans and, for the majority that are, these largely focus on their previous or future plans. The majority lacked detail on areas such as performance trends and, again, often did not report if savings were recurring or non-recurring.

32. Councils have identified the need to generate future savings as they undertake wider-scale transformation, redesign how services are delivered and consider their future policies on fees and charges for accessing services. This will need to be done in consultation with their partners and citizens. Councils should report more transparently the nature of their savings and how these could impact services on an ongoing basis.

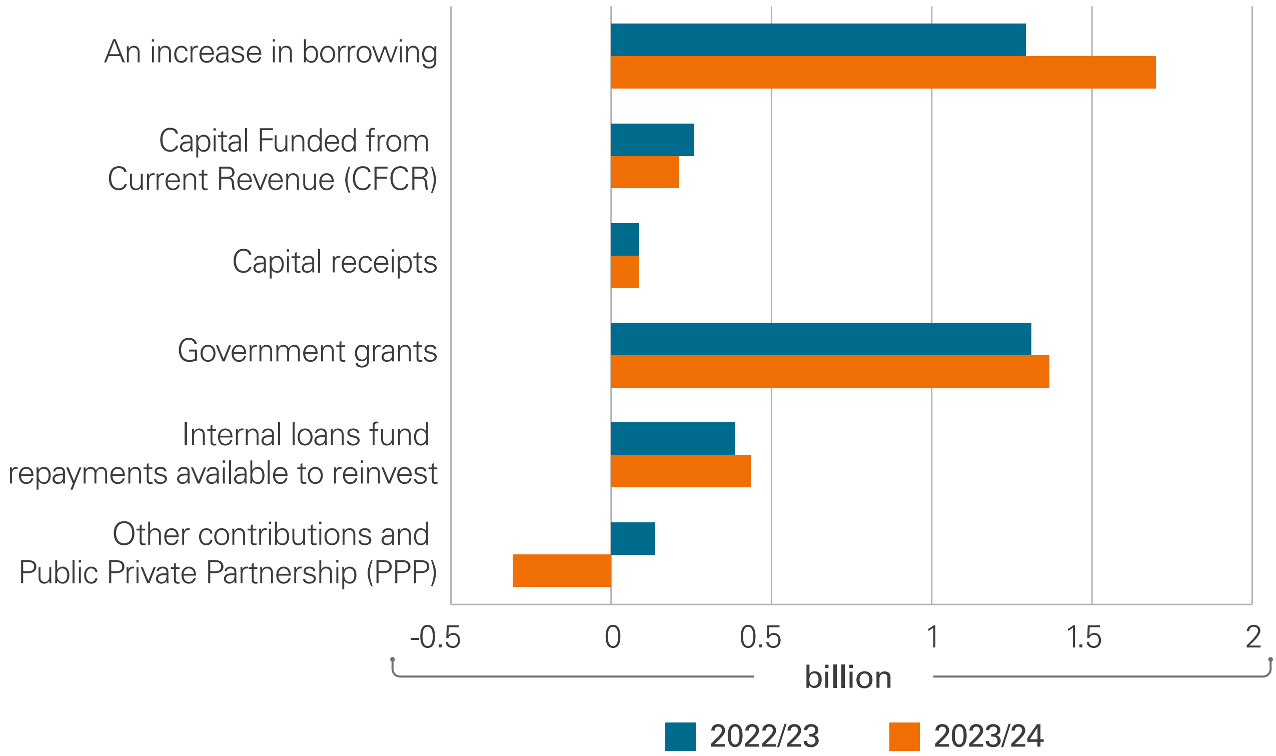
Capital expenditure was 20 per cent lower than planned and funded by increased borrowing

33. The value of council estates, mainly council owned property (including buildings and schools) and equipment, increased by £5 billion in 2023/24 to £51 billion. This reflects continuing investment by councils and, in 2023/24, capital expenditure was £3.5 billion. This is comparable in cash terms to 2022/23. Borrowing increased again in 2023/24 to £1.7 billion, a significant increase of £406 million (31 per cent) since 2022/23, and up £1.2 billion (196 per cent) since 2018/19. Borrowing was used to finance 49 per cent of total capital expenditure (Exhibit 6, page 21).

34. From our sample of 30 councils providing information through the data return, 25 reported a capital underspend in 2023/24 of £755 million. This equates to 20 per cent of councils' total capital budget. This is less than the underspend of 24 per cent in 2022/23; however, it is still higher than the 17 per cent reported in 2018/19. Significant underspends were reported for both General Fund (23 per cent of budget) and HRA capital programmes (15 per cent of budget). Councils reported a range of project types and reasons for why capital underspends had occurred (Exhibit 7, page 21).

Exhibit 6.
Capital expenditure split by sources of finance, in cash terms

Borrowing and government grants remain the most significant means of financing capital investment.



Note: Internal loans fund repayments are an annual charge that recognise capital costs in the revenue budget. Once repaid, they allow borrowed funds to be used elsewhere. Capital receipts are income councils generate from selling existing assets. Revenue transfers is capital expenditure funded from service revenue budgets.

Source: Councils' annual accounts 2022/23 and 2023/24 (audited and unaudited)

Exhibit 7.
Type and reasons for underspends on councils' capital programmes

	Project type	Reasons for
 **Underspends**	• School and early learning building projects. • Housing projects. • Large-scale infrastructure projects (with a small number of councils underspending in relation to projects being delivered as part of their City Deals).	• Project and programme slippage, caused by a range of supply chain and capacity issues. • Project delays caused by cost, contract and legal negotiations and unexpected issues arising during the course of works. • Project deferment.

Source: Council data returns

35. Managing their capital programmes is an important tool for councils to control their annual expenditure. All but two councils reported having a multi-year capital plan in place. These covered a range of periods from five to 30 years, with most covering five to ten years. South Lanarkshire and Stirling councils both reported only having an annual capital plan in place. A multi-year plan allows councils to manage their capital spending over this period.

36. However, consistently failing to invest in estates and infrastructure increases the risk that asset failures may impact services, projects will become more expensive to deliver, and that maintenance spending will need to increase due to assets becoming older. It also impacts the ability of councils to manage their overall estates, identify surplus assets and consider the efficiency of partnership working, including co-location with other services.

Borrowing means debt has again increased, and further borrowing will be needed to invest in new schools

37. Due to the increased reliance on borrowing to fund investment, councils' net debt has now risen to £19.8 billion. This is an increase of 15.8 per cent from 2022/23 and a 29.7 per cent increase since 2018/19. All but one council increased their debt in 2023/24. The cost of servicing debt has risen, with a 16 per cent rise in interest payable and similar charges since 2022/23. Interest payable as a proportion of net cost of services, was six per cent compared to five per cent in 2022/23.

38. Under **LEIP**, councils borrow to meet the cost of building new schools, with the Scottish Government providing revenue grant funding over a 25-year period linked to specific outcomes (maintenance, energy efficiency, digital infrastructure and job creation) to meet maintenance and life-cycle costs. Councils, however, need to fund the £1 billion cost of building schools, including any interest on the money borrowed to fund this. The programme has faced significant delays and cost increases and, to complete the programme by the planned date of 2027, significant further borrowing by councils will be needed.

39. Alongside investing and maintaining their own estates, councils have made use of a range of different Public Private Partnership (PPP) contracts to invest in their estates. A number of earlier Private Finance Initiative (PFI) contracts are now nearing the end of their terms. Councils are having to prepare for, and manage, complex closing arrangements. Councils have already entered into negotiations relating to contracts that are ending, with 10 PFI contracts due to expire by the end of 2030.

In September 2019, the Scottish Government announced it would support £1 billion of capital investment in the school estate on a match-funding basis. In consultation with councils, this created a joint £2 billion **Learning Estate Improvement Programme (LEIP)**, enabling additional investment without the use of private finance contracts. Councils provide upfront capital funding and Scottish Government revenue follows over 25 years for achievement of outcomes.

40. By making use of **financial flexibilities** across 2022/23 and 2023/24, councils have been able to reprofile the debt associated with PPP contracts. This has allowed councils to recognise significant gains from annual contractual payments they have previously made, recognising these within their usable reserves. Future capital expenditure will be able to be offset against these, but they are not cash backed. This means the need for councils to borrow to finance their future capital investment has not changed, nor have their current external debts. Alongside LEIP projects, councils have already committed to significant future borrowing.

41. Councils set and agree their borrowing and treasury management strategies individually, deciding on what is a prudent and affordable level of debt under the Prudential Code. As part of this, a range of indicators are considered, including the cost of servicing their debts, to show that capital plans are affordable and sustainable. Increased borrowing means increased costs that will need to be met annually from revenue budgets. While auditors have not expressed specific concerns about the level of borrowing (in the 15 annual audit reports that were available at the time of our review), it is a factor in the assessment of financial sustainability and auditors are expressing greater concerns about the overall financial sustainability of councils (paragraph 58).

Between 2020 and 2024, the Scottish Government permitted councils to make use of a range of **financial flexibilities** to manage financial pressures. One of these related to service concessions (including PPP) and allowed councils to reprofile debt repayments. This offered an immediate benefit of significant one-off increases to reserves but these are not cash backed, and debt payments will need to be made for longer, deferring costs to later years which has implications for future revenue budgets.

3. Financial position and outlook

Using reserves to manage financial pressures and stay within agreed budgets is not sustainable. Usable reserves fell in 2023/24, and most are committed for specific purposes. Progress on transformation and reform must be prioritised to ensure longer-term financial sustainability.

Councils' usable reserves remain higher than before the pandemic, mainly due to the use of financial flexibilities, but decreased in 2023/24

42. Holding and using reserves is a normal, and helpful, way of managing council finances but reserves are a one-off resource meaning councils need to carefully plan and monitor how these are being used. Using reserves to support services in the short term is not sustainable unless they are used to support service transformation and generate future savings.

43. In 2023/24, councils' total usable reserves decreased by five per cent to £4.1 billion which equates to around 25 per cent of net cost of services. The overall decrease is attributed to a fall in capital reserves along with a very modest increase in revenue reserves (Exhibit 8, page 25).

44. Usable reserves remain £1.66 billion higher than before the pandemic. Revenue reserves were boosted in recent years by:

- Covid-19 funding, but these are largely exhausted with only around £67 million remaining earmarked (2.8 per cent of the committed General Fund balance)
- making use of financial flexibilities related to service concessions, resulting in reprofiled debt and significant one-off increases to reserves. Although an accounting adjustment, and not cash backed, these can be used to support services.

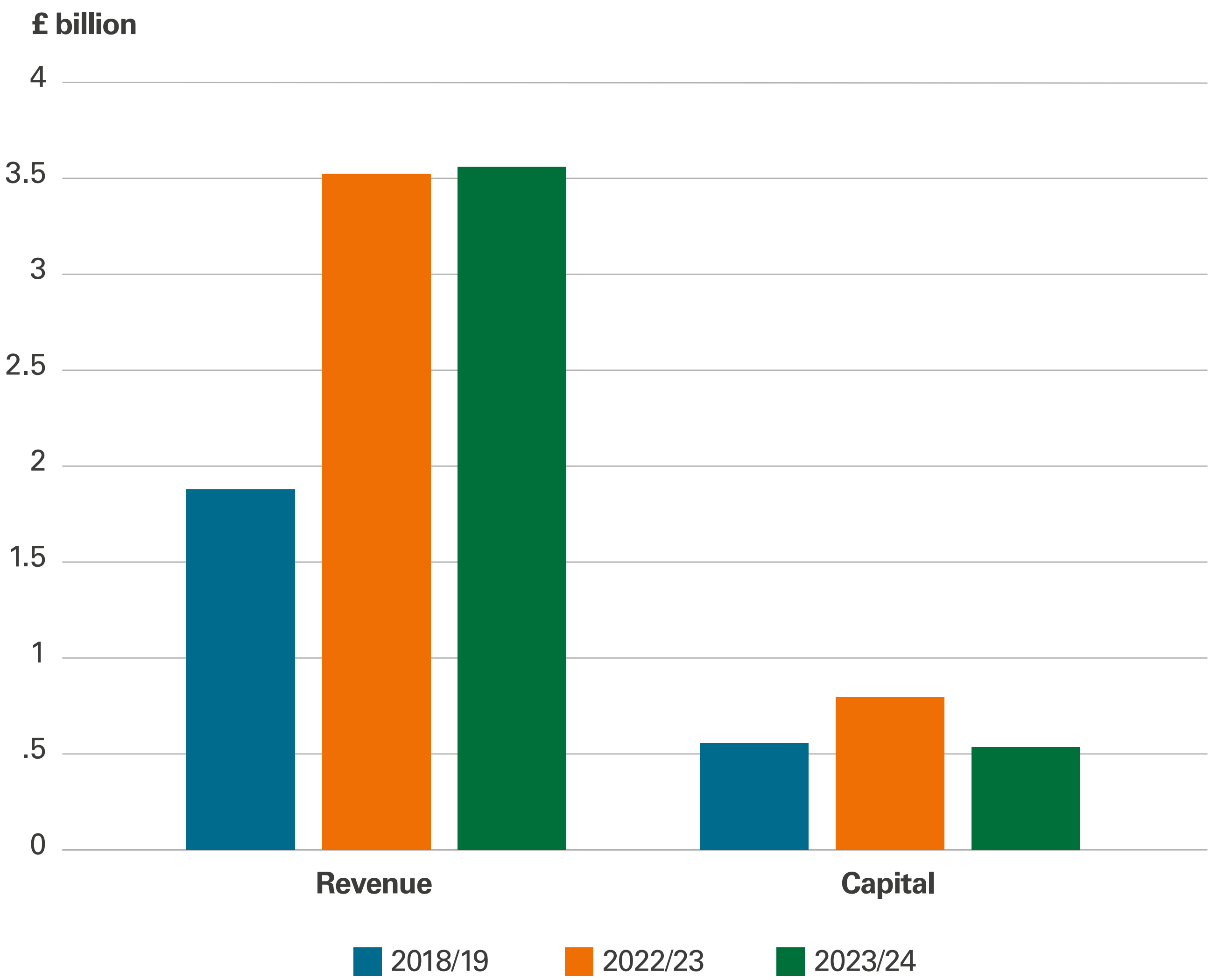
Usable reserves can be used to support service delivery, and to meet in-year expenditure (and are sometimes referred to as cash backed reserves).

Unusable reserves represent accounting adjustments to reflect things such as an increase in the value of council-owned buildings. They generally cannot be routinely accessed or used to support services.

Exhibit 8.

Councils' usable reserves, 2023/24 compared to 2022/23 and 2018/19

Revenue reserves are higher than pre-pandemic but have remained relatively static in the last year.



Note: Total usable reserves were £4.1 billion in 2023/24. Between 2022/23 and 2023/24 revenue reserves increased by 0.8 per cent, capital reserves fell by 33 per cent. Total usable reserves are 68 per cent higher than in 2018/19, up from £2.4 billion (90 per cent increase in revenue reserves, four per cent decrease in capital reserves)

Source: Councils' annual accounts 2023/24 (audited and unaudited)

45. The overall decrease in usable reserves in 2023/24 is notable as they have been increasing significantly in recent years. Two-thirds of councils still increased their total usable reserves, but this is largely attributable to councils making use of financial flexibilities (a number of councils accounted for this in 2022/23, while others introduced it in 2023/24).

46. Around a third of councils saw their total usable reserve fall in 2023/24, including some large decreases related to the drawing down of committed reserves. These reserves were used for Equal Pay settlements, pay awards, budget support and the further deployment of Covid-19 reserves.

General Fund reserves increased slightly but over 80 per cent are committed for specific purposes

47. General Fund reserves (excluding the HRA element which not all councils have) continued the upward trend of the past five years, increasing by three per cent in 2023/24 to £2.8 billion. This equates to 17 per cent of net cost of services and is driven by growth in **committed reserves**. **Uncommitted reserves** have remained constant at between two and three per cent of net cost of services (Exhibit 9, page 27).

48. In 2023/24, over 80 per cent of the General Fund was committed. This means that it has been allocated for specific purposes and is not readily available for other uses.

The **General Fund** is the principal usable revenue reserve held by councils. It can be used for a wide range of purposes, including bridging budgets gaps as it can be used to finance spending on services or some elements of capital spending.

The Housing Revenue Account (HRA) reserve can only be used to fund spending on council-owned housing.

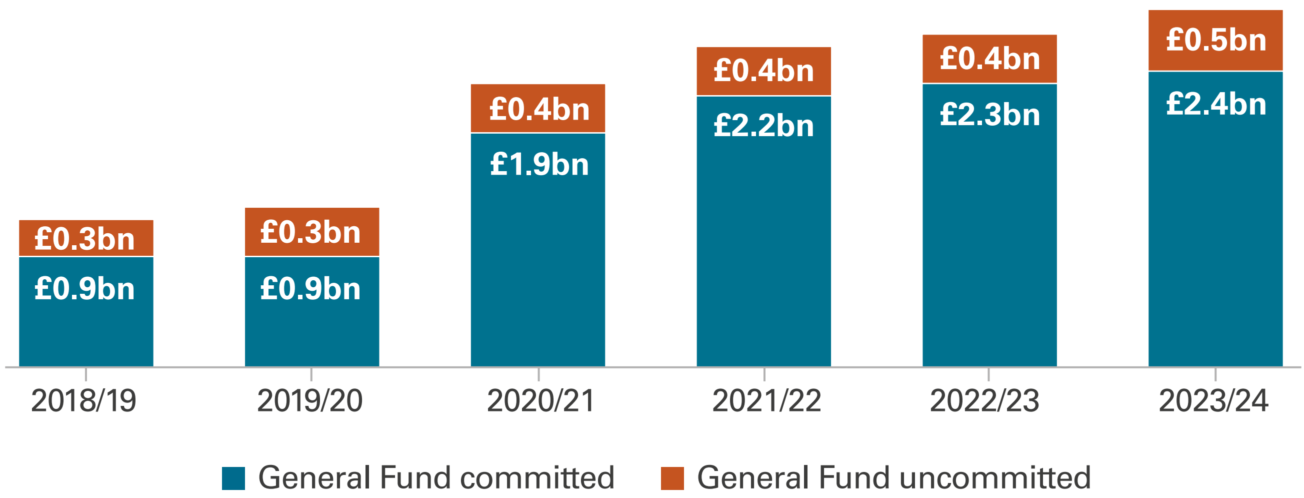
Committed reserves have been allocated (or earmarked) for specific purposes and are not readily available for other uses.

Uncommitted reserves can be deployed more easily and, because of the nature and scale of it, the uncommitted element of the General Fund can be considered to represent a degree of contingency funding.

Exhibit 9.

Councils' General Fund balance between 2018/19 and 2023/24, split by committed and uncommitted

General Fund reserves are increasing but over 80 per cent is committed.



Source: Councils' annual accounts 2023/24 (audited and unaudited)

Some councils' levels of uncommitted reserves are low, but they have specific reserves earmarked for contingency

49. Councils have reserve policies in place, which set out the rationale for the minimum level of uncommitted reserves held by the council. Most have an agreed minimum level, usually two per cent of their net budgeted revenue expenditure, although four councils have set this higher.

50. In 2023/24, nine councils had an uncommitted reserves level of less than two per cent of net budgeted revenue expenditure. However, a review found that in many cases these low reserve levels were planned decisions and the levels were deemed to be sufficient and/or supported by additional committed funds for contingencies. Aberdeenshire, South Ayrshire and West Dunbartonshire all had uncommitted reserves below their minimum level and intend to review this during 2024/25.

51. While councils hold uncommitted reserves for contingencies, around a third reported also earmarking some reserves specifically for contingencies to either manage budget risks or specific risks, such as adverse weather. The nine councils providing information on the value of the reserves earmarked for contingencies reported a total of £50 million.

Councils continue to use their reserves to manage budget pressures, but this is not sustainable

52. While overall usable reserves levels remain high, there is evidence that councils are continuing to use reserves to support service spend and this is not sustainable. In 2023/24:

- Councils bridged over a quarter of their budget gap using reserves (£202 million).
- Twelve councils reported making unplanned use of reserves in 2023/24, to support in-year spending and to balance the outturn position. This was most often to cover the cost of the 2023/24 pay award; to address specific service or project pressures, or to provide financial support to IJBs.

53. Usable reserves held as a proportion of spending has reduced. In 2023/24, 15 councils held usable reserves that were over 20 per cent of their net cost of services, which is less than 2022/23 (20 councils) but still higher than before the pandemic (nine councils). This indicates that reserves are increasing at a slower rate than expenditure, even with use of financial flexibilities. One council had total usable reserves of less than ten per cent of their net cost of services.

Councils could improve how clearly they report on how they intend to use their reserves

54. With the use of reserves to support services and the low level of uncommitted reserves across the sector it is increasingly important that councils report how and when the intend to make use of their reserves (Case study 1, page 29).

Case study 1.
Councils could be more transparent within their published plans about how they intend to make use of reserves

A review of councils' management commentaries found that all councils clearly identify key areas of reserves and explain their purpose, with most identifying their minimum reserve level.

All but two councils reported, through their data return, that they formally document or publish at least some information about their committed reserves. Committed reserves information is usually documented in councils' accounts or financial outturn reports, and sometimes in other formats, such as reserves reports. Few councils reported documenting information in performance monitoring reports.

Nearly all councils publish and document a full costed breakdown of committed reserves categories and details of what has been drawn down within the year. Although most formally document what is committed for major initiatives, this information is not always published. Only two thirds of councils document or publish information on planned spend for future years.

Source: Council data returns and Council annual accounts 2023/24 (audited and unaudited)

Recent changes to pension contribution rates offer councils a short-term window to reduce costs

55. The result of the 2023 triennial revaluation showed a significantly improved funding position across Scotland's 11 local government pension funds. Councils are using this as an opportunity to lower their employer contributions and reduce their costs in the short-term. The 12 councils who are members of Strathclyde Pension Fund are reducing their contribution rates from 19.3 per cent to 6.5 per cent for 2024/25 and 2025/26 (increasing to 17.5 per cent in 2026/27), significantly reducing their annual contribution costs for two years. Other councils are making more modest reductions to their contribution rates of between two and three percentage points.

Ensuring medium- and long-term financial sustainability is a significant challenge

56. The risks to financial sustainability are well known. These include external factors such as increased demand, demographic changes and the need to invest significantly to address certain policy areas such as climate change and its impact. There are also specific pressures that councils identified as presenting risks to achieving future financial balance/sustainability including:

- **Uncertainty about future funding:** single-year settlements, ring-fencing of funding and directed funding for specific Scottish Government policies limiting local flexibility (for example, teacher numbers, social care provision and IJB allocations).
- **Council tax freezes:** while there is no freeze in 2025/26, the Scottish Government froze council tax between 2008/09 and 2016/17, and in 2021/22, and capped increases at three per cent in 2017/18 and 2018/19. The risk of future freezes is seen as a main challenge to ensuring medium- to long-term financial sustainability. Even when 'fully funded' a council tax freeze suppresses the growth of the council tax base over that period and the income generated when the freeze is lifted is lower than if councils were able to make tax-raising decisions at a local level.
- **Pay awards and employers' NI costs:** overspends have been caused by pay awards, with some councils reporting that the budgets provided are not enough to cover the costs or these costs are unfunded. In 2023/24, three councils made unplanned use of reserves to meet pay awards and there is ongoing uncertainty about the scale of future annual offers. There is now also uncertainty over how increased employers' NI contributions will be funded.
- **Inflationary pressures:** general pressures and some specific issues that impact the delivery of capital programmes (costs of goods and services, service demand, public perception, borrowing, funding, increasing standards and difficulty with asset sales).
- **Savings:** some councils cited the challenge of identifying and achieving recurring savings.

57. Most councils reported that financial sustainability was a significant challenge. Some specific challenges reported by councils include:

- Angus Council reported the need for change if they are to be financially sustainable over the medium to long term. The scale of reductions required could leave some services unable to function.
- East Lothian Council identified critical risks to its fiscal sustainability and reported managing their financial environment as the highest ever scoring risk on their Corporate Risk Register.
- Inverclyde Council reported that ongoing depopulation may mean significant future funding reductions.
- Orkney Islands Council highlighted the growing contribution from reserves to meet in-year service costs as being unsustainable.
- Shetland Islands Council reported they were financially unsustainable on the basis of current plans.

58. Alongside councils' own assessment of their financial sustainability, many auditors highlighted in their 2023/24 annual audit reports (15 available for review) the challenges councils face in achieving financial balance in future years and securing long-term financial sustainability. These centred on the scale of budget gaps; the need to keep on top of savings plans; low levels of uncommitted reserves; unsustainable cost bases and the difficult choices to be made.

Councils have medium-term financial plans in place but must now make progress on transformation and reform

59. While several councils reported confidence that they had robust processes and actions in place to ensure they were financially sustainable, councils largely reported that it is difficult to plan into the future without clarity on medium- or long-term government funding and priorities, stating there is general economic uncertainty and volatility. This difficulty, however, underlines the importance of councils ensuring that they have a clear understanding of risks to their financial positions, effective risk management processes to monitor these, and indicative forecasts informed by scenario planning.

60. All councils that provided data returns to us reported having medium-term financial plans in place, with most of these spanning 3-5 years (25 out of 30 councils). Most councils (25) reported that they reviewed their financial plans in 2024. Half of councils (15 out of 30) have a long-term financial plan in place and, for those that do, most cover a 10-year period.

61. As we set out in our recent Transformation in councils report, councils must prioritise and progress the delivery of their plans for transformation. And a step change is needed in terms of scale and pace. That could look like new innovative approaches to service delivery, reconsidering which services could be more effectively delivered by other partners, exploring opportunities for new income generation (including those that are being legislated for) or identifying how economies of scale could be achieved by sharing services.

Transformation is our next Best Value thematic focus and we will be auditing councils' plans for transformation as part of the 2024/25 annual audit.

62. Delivering transformation successfully requires resources to be committed towards it and it is positive to see that most councils (27 from our data return sample of 30) reported holding reserves earmarked for transformation. Glasgow, Orkney and Shetland did not. Of the 26 providing information on the value held, a total of £270 million was reported which is about 13 per cent of committed General Fund balance and equates to two per cent of the net cost of services. Most councils' transformation reserves were equivalent to two per cent or lower of net cost of services, but some earmarked a significantly higher proportion. Argyll and Bute earmarked the equivalent of ten per cent of net cost of services, Scottish Borders six per cent, and Aberdeenshire, East Lothian and Highland all earmarked five per cent.

Councils could make more use of financial sustainability indicators, including to inform their longer-term planning

63. Assessing and monitoring financial sustainability is essential. Councils use a range of indicators to do so, but the type used, and extent of their use, varies. The Local Government Benchmarking Framework includes sustainability indicators, currently being reviewed by Directors of Finance, to ensure that they remain appropriate, and CIPFA also recommends indicators. Councils are not required to use specific indicators and have discretion as to how they assess their own financial sustainability.

64. We asked councils how they assess and monitor financial sustainability, including how this is reported to elected members:

- Around three-quarters of councils use the Local Government Benchmarking Framework Indicators and the CIPFA level of reserves indicator.
- Around a third of councils use the CIPFA change in reserves and reserves sustainability measures.
- Some councils reported that they use their own equivalent calculations or different indicators including outturn against expenditure, ratio of council tax to overall funding, ratio of financing costs to net revenue stream, external debt and borrowing levels, and recurrent versus non-current budget mitigation.

65. Most councils reported that they assess and monitor financial sustainability more generally, such as via the regular monitoring of budgets, reserves and the capital financing requirement; and carrying out periodic risk assessments. For example, East Ayrshire Council's 'East Ayrshire Performs' reports financial and service performance information about the council publicly, including a suite of financial resilience indicators, focusing on council reserves and liquidity but also capital financing, investment and borrowing.

66. Most councils include and consider financial indicators within their financial plans, with 17 councils including an analysis of financial sustainability and/or resilience indicators within their medium-term financial plans and nine within their longer-term plans.

67. All councils reported to us that elected members had been provided with a summary of the council's medium- to long-term financial sustainability but more needs to be done to regularly and formally report upon the consideration of financial sustainability. This should be reported publicly, as a minimum, as part of annual budget-setting papers and within annual refreshes of financial plans.

Financial outlook

68. Within this report we outline the financial challenges Scotland's councils are now facing. While indications are that the 2025/26 budget will result in increased funding, and councils are now free to vary council tax rates, it is unlikely that increased funding and income will be able to keep pace with increasing costs. In recent years councils have been able to increase the reserves they hold, but much of this has been due to additional Covid-19 funding, use of financial flexibilities and other one-off actions. The initial benefits of these measures, and the reserves that councils were able to build, do not negate the need for significant reform and transformation. 2023/24 saw a reduction in usable reserves and while this represented only five per cent of these reserves, this was equivalent to over eight per cent of the usable reserves held as recently as 2019/20.

69. How councils plan to use their reserves, make savings and transform their services needs to become more transparent as financial sustainability issues are to be addressed. The need to consult local communities and clearly communicate the implications of budget decisions has never been more important.

70. Our next Local government in Scotland publication, Local government budgets 2025/26, will examine the steps that Scotland's councils take as they set their budgets for 2025/26, setting out the finalised funding settlement from the Scottish Government, decisions taken in setting council tax and the steps they intend to take to fund and transform services.

Appendix 1

Progress against the recommendations in Local Government in Scotland Financial Bulletin 2022/23

Councils should:	Progress/ status
Prioritise the achievement of recurring savings and avoid reliance on non-recurring savings to enhance longer-term financial sustainability	**In progress/Limited progress** The overall extent of progress against this recommendation is difficult to assess due to a lack of detail and transparency in reporting on recurring and non-recurring savings performance (paragraph 30). An updated recommendation on savings performance and transparency is included in this report.
Ensure that management commentaries are open and transparent, include a clear link between budget outturn and the financial performance in the accounts and report on the achievement of planned savings targets	**In progress** Our review of 2023/24 management commentaries found that that most councils reported outturn against budget with significant variations explained. However not all councils provided sufficient information on savings target achievement. An updated recommendation on savings performance and transparency is included in this report.
Provide clear statements about reserves policy and explicitly set out the purpose of committed reserves within their annual accounts. This will enhance the level of assurance that councils can provide regarding their ongoing financial sustainability	**Complete / In progress** A review of available councils' management commentaries found that key areas of reserves were clearly identified, with the purpose explained and the majority identifying a minimum reserve level. However publication of committed reserve information was less well evidenced (Case study 1). An updated recommendation on greater transparency of reserves is included in this report.

Cont.

Councils should:	Progress/ status
Ensure effective and timely consultation and engagement with communities on the options that must be considered to achieve a balanced budget	**In progress** Less than half of councils stated, via our data return, that public consultation was undertaken when preparing budgets for 2023/24. In our Local government budgets 2024/25 publication, 24 out of 32 councils stated they undertook community engagement on financial pressures. We will follow this up in our budget briefing in Spring 2025 when we look at councils' 2025/26 budget setting.
Strengthen their monitoring and reporting of financial resilience including clearer and more public-facing use of performance against financial resilience indicators and measures. Financial resilience indicators should be a component of councils' medium and longer-term financial plans to provide assurance that they are balancing short-term pressures with robust planning for long-term financial sustainability	**In progress** Most councils reported that they assess and monitor financial sustainability, with financial indicators used in financial plans, with 17 explicitly using these within their medium- and long-term financial plans (paragraphs 63 - 67). An updated recommendation on the use of financial indicators in monitoring and reporting is included in this report.
Work with the Scottish Government to build momentum and accelerate progress in the development of a fiscal framework for local government to enhance the clarity and certainty of budgets for councils in future years	**In progress** We understand that COSLA and the Scottish Government have been progressing the development of a fiscal framework

Local government in Scotland

Financial bulletin 2023/24

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