

Progress Publication, December 2023: Fiscal Framework between Scottish Government and Local Government

December 2023



Joint Foreword

In June of this year, Local Government and Scottish Government committed to improving our partnership working and to addressing three shared priorities – poverty, net zero and sustainable public services. In signing the Verity House Agreement, we jointly accepted that changes were required to our relationship - the way we work together, how we will approach our shared priorities, and how we engage with each other in a positive and proactive manner.

We recognise that in the period since signing, there have been challenges and disagreements, but that those have made it even more important for us to deliver on actions set out in the Verity House Agreement. Among those is the commitment to deliver a Fiscal Framework between local and national government.

The commitment to deliver a fiscal framework was first made in December 2019, but progress paused during the Covid Pandemic, as both spheres of government prioritised our pandemic response and recovery. Since early 2022, discussions have recommenced, and good progress has been made. It was identified as essential that the partnership agreement take precedence, to agree what our priorities were and how we would deliver them, and to then focus on developing and agreeing a fiscal framework.

We are pleased that progress has been made on a draft framework, and some of this has already been put into practice including improved evidence-based pre-budget discussions and joint working to consider new local taxes and reform of existing local taxes.

However, there remains more to do. We both acknowledge that there is a need to consider the options and impacts of a *rules-based approach* to setting the budget for local government, and joint exploration of that is ongoing. It is essential that, if such an approach is taken, we get it right given the sums of money involved, and therefore will take more time.

To demonstrate the progress we have made, and to affirm our commitment, we are publishing this report, but we are already putting the principles and approach set out into practice.



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COSLA Resources Spokesperson



Shona Robison
Deputy First Minister and Cabinet
Secretary for Finance

Progress Report on the work to develop and agree a Fiscal Framework between Scottish Government and Local Government

Note: This document is a progress report on a working draft which remains subject to change in the light of completion of the document as a whole, and eventual consideration by the appropriate governance mechanisms in both the Scottish Government and Local Government.

Introduction

The Verity House Agreement, signed on 30 June 2023 as part of the New Deal with Local Government, committed to concluding a Fiscal Framework which establishes early and meaningful budget engagement, the simplification and consolidation of the Local Government Settlement, and establishes a clear process for exploring local revenue raising powers and sources of funding. The Framework should also, wherever possible, provide multi-year funding certainty to support strategic planning and investment.

Discussions on a fiscal framework have taken place alongside the development of the Verity House Agreement, with some sections nearing completion. There remains work to be undertaken to complete the drafting and reach agreement on a final draft. Nevertheless, both parties are committed to acting in accordance with those parts of the framework which have provisionally been agreed.

The following sections summarise the areas of work which have made the most progress and identifies those areas which are for further development.

Principles and Approach

Central to the fiscal framework is the principle of regular and meaningful engagement, and respect for each other's democratic mandate, in order that we can work together more effectively to improve the lives of people in Scotland.

Further, the Verity House Agreement established a default position from this point forward that there will be no ring-fencing or direction of funding, unless there is a clear joint understanding of and rationale for such arrangements. The Verity House Agreement and the Fiscal Framework should together balance greater flexibility over financial arrangements for local government, with clearer accountability for the delivery of shared priorities.

The Fiscal Framework establishes an agreed foundation for cooperation and coordination on all matters concerning the financial relationship between Local Government and the Scottish Government.

This Fiscal Framework will set out provisions relating to:

- Roles and scope
- Scottish and Local Government Funding
- Local Taxation & Fiscal Flexibilities
- Scrutiny and Accountability
- Governance and Dispute Resolution

The Fiscal Framework will have the status of a 'Memorandum of Understanding', it is a statement of political intent and should not be regarded as a binding agreement, and does not create legal obligations. However, the provisions of the European Charter for Local Self-Government are being considered throughout the design and drafting. In accordance with the Charter, this framework is not intended to constrain the independence of Local Government, or the freedoms of either party to operate in areas for which they are responsible, but rather to enhance the work required to deliver our shared priorities and produce better outcomes for communities.

The underpinning principles of this Fiscal Framework as agreed are:

A – The fiscal framework should promote stability, certainty, transparency, affordability and sustainability.

B – The fiscal framework should promote effective use of fiscal flexibilities and levers to address local priorities and improve outcomes

C – The fiscal framework should enable discussion of fiscal empowerment of Local Government.

Scottish and Local Government Funding

The framework will reflect that the Scottish Government provides local authorities with funding to operate independently through the provision of block grant funding, and to take locally appropriate decisions, openly and transparently, to operate as effectively as possible within that fiscal context. Local authorities also have their own sources of revenue including the raising of Council Tax, discretionary local fiscal levers (for example the Workplace Parking Levy), and the setting of fees and charges for a range of services.¹

The framework will further reflect that it is the role and responsibility of each individual local authority to manage their own budgets and to allocate the total financial resources available to them based on local needs, the fulfilment of any statutory obligations and jointly agreed national and local priorities. The management of the available budget and the effective utilisation of funds to deliver services to local communities are local decisions to be determined by locally elected representatives. From the signing of the VHA forward, decisions on ringfencing and/or restrictions on funding will be taken jointly in accordance with that agreement.

Sources of Funding for the Scottish Government

The framework will reflect the sources of funding that central government has to spend, and the sources of funding which Local Government has to spend. It will set out the interaction between these and how each are set.

The Scottish Government and Local Government acknowledge that single-year budget allocations are sub-optimal across the public sector and our partners, compared with multi-year spending plans which better enable long-term planning.

As the UK Government provides the Scottish Government with an annual resource budget settlement, the Scottish Government does not currently set more than a single year budget (and therefore more than a single year local government finance settlement).

¹ See Annex A

Budget Process and Engagement

Scottish and Local Government are committed to new ways of working in the fiscal relationship going forward, which supports transparency and accountability. This will encourage a relationship based on collaboration and improve our shared information and evidence base. The Fiscal Framework will set out agreement on engagement with regards to:

- high level policy ambitions,
- strategic issues,
- the demands of the previous and current financial year,
- the fiscal and economic circumstances in which decisions must be made for the next financial year,
- horizon scanning and the impacts for medium to long term financial plans.

The framework will establish specific mechanisms and anticipated cycles of meetings to facilitate this engagement tied to key fiscal and policy events over the financial year. See draft Annex B.

There has been progress in agreeing the nature of this process for engagement, and improved budgetary engagement has already begun in 2023-24 with more to begin from the next cycle as this approach is embedded.

The key area outstanding for further development is whether to include a ‘rules-based approach’ to the setting of the Local Government Settlement – further work is underway and will inform future discussions between COSLA Leaders and Scottish Ministers.

Subject to this, further consideration will also be given to the appropriate distribution of risk and responsibility, and the approach to any in-year changes.

Local Taxation and Fiscal Flexibilities

The framework will build on the commitment of the Scottish Government and Local Government to enhancing local fiscal levers and flexibilities through the exploration of new opportunities, and to regularly evaluating existing local levers to ensure they are fit for purpose.

Notwithstanding Local Government’s desire to see more local discretionary powers, we have currently agreed a structured process of design and evaluation of fiscal levers. This will ensure that Scottish Government and Local Government currently have a mechanism to work together to deliver opportunities for fiscal empowerment. The framework will set this out, and key elements of this are already being brought to bear in current joint work to examine new levy and tax proposals, as well as reform of existing local taxes.

Scottish Government and Local Government consider that new fiscal levers, which are created to be administered and levied by Local Authorities, should favour local discretion, unless there is a legitimate reason that policy should be set nationally and there is agreement to that effect.

Monitoring, Reporting, Governance, Review and Dispute Resolution

Further discussion will take place to ensure that there are links between the fiscal framework and the overall outcomes, monitoring and accountability framework to be developed under the auspices of the of the Verity House Agreement.

Consideration is needed as to any additional bespoke governance mechanisms for the fiscal framework which may be required, taking into account and linking into the existing Verity House Agreement engagement mechanisms.

Finally, parties are minded to agree the inclusion of an explicit review provision for the fiscal framework and agreement will be reached about how that should be framed including specific timeframes for implementation.

Annex A – Scottish Government and Local Government Funding

Sources of Funding for the Scottish Government

1. The money that Scottish Government has to allocate, collectively called the Scottish Consolidated Fund, comes from the following sources:
 - a. block grant from the UK Government
 - b. other funding from the UK Government
 - c. Scottish income tax (collected by HMRC)
 - d. non-domestic rates (collected by local authorities and redistributed by the Scottish Government)
 - e. devolved taxes (collected by Revenue Scotland)
 - f. borrowing
2. The block grant includes resource, capital, annually managed expenditure (which can only be spent for the purposes for which it is allocated) and Financial Transactions allocated by UK Government at UK fiscal events and is currently determined with reference to the overarching requirement to meet the objectives set out in the Charter for Budget Responsibility²
3. Changes in the block grant are calculated as a population share of changes in spending on public services devolved to Scotland. These arrangements are set out in the Statement of Funding Policy³ and the allocation process is often referred to as the Barnett Formula.
4. For devolved social security benefits and all taxes set, raised or assigned in Scotland, the block grant is subsequently adjusted to reflect the benefit costs and tax revenues foregone by the UK Government. These 'block grant adjustments'⁴ reflect the hypothetical value that would have been raised or spent in Scotland by UK Government if the taxes and payments had not been devolved.

Sources of Funding for Local Government

5. Local Government receive their funding mainly from the following sources:
 - a. Scottish Government General Revenue Grant (GRG) and General Capital Grant (GCG)

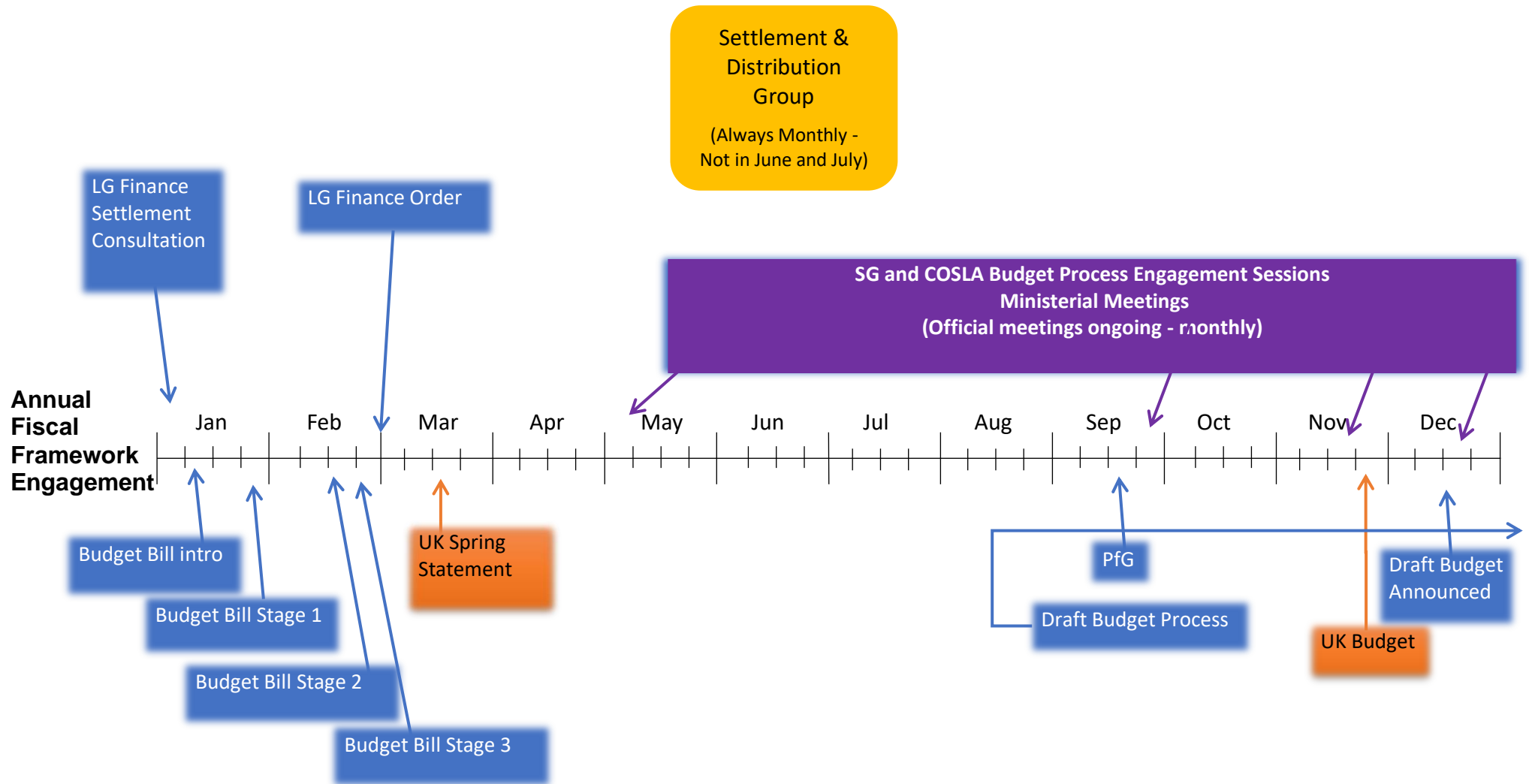
² [Charter for Budget Responsibility: autumn 2016 update - GOV.UK \(www.gov.uk\)](http://www.gov.uk)

³ [Statement of Funding Policy update Feb 2023.pdf \(publishing.service.gov.uk\)](http://publishing.service.gov.uk)

⁴ [Block grant adjustments - Fiscal framework: factsheet - gov.scot \(www.gov.scot\)](http://www.gov.scot)

- b. Non-domestic rates (collected by local authorities and redistributed by the Scottish Government)
 - c. Council Tax (collected by local authorities)
 - d. Government Grants (other than GRG and GCG) from either the Scottish or UK Government.
 - e. Other Grants including from NHS Boards and income from Integrated Joint Boards
 - f. Customer and Client Receipts, from fees and charges for services.
6. The Scottish Government guarantees each local authority receives the total level of funding set out in the local government finance settlement (detailed in the Local Government Finance Order and circulars) through a combination of General Revenue Grant plus Non-Domestic Rates Income, and each councils' share is calculated using the jointly agreed needs-based formula.
7. An adjustment to each councils' funding is made which assumes a baseline level of Council Tax receipts. This takes into account local authorities' differing tax bases, but also enables councils to raise additional funding to spend on local services.

ANNEX B - Fiscal Framework (FF) – Fiscal Events and SG and LG Budget Engagement Process





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