Local Government Debt in Scotland

Report for the Green MSPs

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Contents

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What is it, and why is it a problem?

Local authorities across Scotland are in large amounts of long-term debt[1]. For most local authorities, this debt is made up of loans from the Public Works Loan Board (PWLB), and 'Lender Option, Borrower Option' (LOBOs) loans from banks.

The PWLB is a statutory body and executive agency of HM Treasury, which considers loan applications from local authorities and collects repayments on any loans that are made. In 2010, George Osborne increased the interest rate on fixed rate PWLB loans - this encouraged local authorities to take on high-risk LOBOs from banks, and removed large amounts of local authority debt from the Central Government balance sheet.

LOBOs are very long-term loans provided by banks, often lasting between 40 and 70 years – on average twice the lifetime of government loans. They are initially offered on a fixed interest rate, known as a 'teaser' rate, which typically undercuts that offered by the PWLB. At pre-determined periods after this, the lender can opt to propose – or impose – new fixed rates. The borrower can either opt to accept the new rate or repay the entire loan. A second type of LOBO, the 'inverse floater', attaches the post-teaser interest rate to market rates.

Some councils are facing 7 – 9 % interest rates on LOBOs, more than twice the current rate of lending at the PWLB. Many local authorities have been unable to take advantage of recent record low interest rates, as exiting LOBOs would incur large fees - twice as much as the exit fees for a government loan.

Estimated earlier this year, an average of 42% of the money raised locally through council tax in Scotland is paid back to HM Treasury, or to banks as repayment for LOBO loans or Private Finance Initiatives (PFIs). Many local authorities spend a significant percentage of their council tax income[2] on servicing this debt: Glasgow City Council spends 55%, whilst Comhairle nan Eilean Siar spends 103% of its council tax income on servicing this debt.

Scotland has the highest proportion of PFI/PPP debt per capita in the world, and 3 of the top 10 LOBO loan borrowers are Scottish local authorities.

Many banks which lend LOBOs are also involved in structuring tax avoidance schemes which provide multinational firms with routes to avoid tax payments, and these banks profit from this provision of advice through fees. Central and local government budgets face gaps in revenue which are created by the tax avoidance banks facilitate – banks then offer to fill these revenue gaps, in the form of LOBOs and PFI schemes. In 2015, it was estimated that banks 'earned more than £1 billion in upfront profits from LOBOs, while the cost to Councils to exit the contracts today could be more than £8 billion.' Last year, Scottish local government revenue grant was cut by between 5% and 7% in real terms, and this remains an area of unprotected spend. Job losses and cuts in service provision have negatively impacted on

[1] You can find out the composition of any local authorities' debt at http://lada.debtresistance.uk/
[2] Council tax contributes around £12 million, or 12%, to total Local Government revenue. See The Commission on Local Tax Reform, Volume 1 – Just Change: A New Approach to Local Taxation, p. 10

some of the poorest and most vulnerable populations, and particularly on women, in Scotland. The level of debt repayments that local authorities make on PWLB and LOBO loans is clearly unsustainable, and especially so in a context of austerity.

Local Authority	Total Long Term Debt	PWLB Debt	LOBO Debt	% of council tax revenue spent servicing debt	
Aberdeen City Council	£483,074,000	£389,179,000	£93,893,000	30%	
Aberdeenshire Council	£504,945,000	£409,345,000	£95,600,000	32%	
Angus Council	£160,480,000	£130,480,000	£30,000,000	37%	
Argyll & Bute	£152,997,000	£100,221,000	£51,277,000	42%	
Clackmannanshire Council	£108,145,000	£84,645,000	£23,500,000	51%	
Comhairle nan Eilean Siar	£147,364,000	£146,364,000	£1,000,000	103%	
Dundee City Council	£404,406,000	£364,406,000	£40,000,000	55%	
Dumfries and Galloway	£153,292,000	£128,746,000	£15,000,000	36%	
East Ayrshire Council	£334,481,000	£267,881,000	£66,600,000	48%	
East Dunbartonshire Council	£141,519,000	£109,383,000	£24,136,000	32%	
East Lothian Council	£331,930,000	£292,630,000	£39,000,000	36%	
East Renfrewshire Council	£68,083,000	£53,541,000	£14,542,000	26%	
Edinburgh City Council	£1,396,544,000	£1,113,688,000	£280,900,000	50%	
Falkirk Council	£202,630,000	£176,630,000	£26,000,000	44%	
Fife Council	£689,794,000	£260,194,000	£357,350,000	47%	
Glasgow City Council	£1,403,240,000	£954,240,000	£449,000,000	55%	
Highlands Council	£746,187,000	£628,131,000	£118,056,000	54%	
Inverclyde Council	£214,273,000	£111,373,000	£102,900,000	54%	
Midlothian Council	£197,969,000	£177,969,000	£20,000,000	40%	
Moray Council	£156,136,000	£122,736,000	£33,400,000	44%	
North Ayrshire Council	£225,354,000	£165,254,000	£60,100,000	40%	
North Lanarkshire Council	£506,974,000	£407,974,000	£98,000,000	39%	
Orkney Council	£40,000,000	£40,000,000	£0	17%	
Perth & Kinross Council	£243,045,000	£194,532,000	£43,513,000	26%	
Renfrewshire Council	£225,556,000	£172,640,000	£52,916,000	34%	
Scottish Borders Council	£170,631,000	£127,631,000	£43,000,000	26%	
Shetland Council	£31,000,000	£31,000,000	£0	27%	
South Ayrshire Council	£177,196,000	£128,991,000	£40,205,000	32%	
South Lanarkshire Council	£1,083,722,000	£1,064,222,000	£17,000,000	56%	
Stirling Council	£126,338,000	£125,072,000	£1,266,000	37%	
West Dunbartonshire Council	£234,361,000	£106,261,000	£92,600,000	61%	
West Lothian Council	£479,376,000	£418,796,000	£60,580,000	46%	
Total	**£11,541,042,000**	**£9,004,155,000**	**£2,391,334,000**	**Average**	**42.42%**

Sources: *Does Your Council Have LOBOs?* http://lada.debtresistance.uk/; Joel Benjamin, (2016), *Forget Tax Hikes: plan B is citizens' debt audit,*: https://www.opendemocracy.net/uk/joel-benjamin/forget-tax-hikes-plan-b-is-citizens-debt-audits[3]

[3] This report distinguishes between long-term debt from PWLB and LOBO loans, and short-term debt, which for most local authorities is a relatively small figure. Audit Scotland (page 18) lists Scottish local authorities' net debt – the difference between what is borrowed and owed (£15.2bn) and the value of short-term investments (£1.4bn) – as totalling £13.8bn, and total short and long-term debt as £12.5bn.

What can be done?

There is precedent for local authority debt cancellations. In 2001, billions of pounds of local authority housing debt were written off by the UK Government – albeit in return for transferring housing stock to community ownership.

Joel Benjamin argues that 'an amnesty on interest repayments on money borrowed by Scottish local government (mostly money borrowed from ourselves!) would save councils £883 million a year, far more than the £604 million cut on the horizon in 2017'.

The crisis facing local authority finances, the unsustainable, unethical and potentially illegal nature of the debt that is precipitating this, and the significant negative impacts that this is already having across Scotland, justifies a cancellation of local authority debt.

LOBOs

In 2008, the UK Government bailed out a range of financial institutions with approximately £500bn of cash and liabilities. The austerity-induced gaps in revenue which local authorities are now facing were caused by the reckless behaviour of many of the same banks which are now lending to local authorities at exorbitant rates.

The levels and form of this debt meet the criteria outlined by Greece's Truth Committee on Public Debt for 'illegitimate', 'odious' and 'unsustainable' debt. This debt is based on grossly unfair terms, violates democratic principles – being against the interest of the population of the borrower, and leading to policies which are not in this population's interest – and is debt which cannot be serviced without seriously impairing the ability or capacity of local authorities to fulfil basic human rights obligations. HM Treasury's own guidance for managing public money states that 'public sector organisations may borrow from private sector sources only if the transaction delivers better value for money for the Exchequer as a whole'[4].

This debt may also meet the criteria for the Truth Committee on Public Debt's classification of 'illegal' debt. As a use of derivatives by local authorities, LOBOs are potentially unlawful and could be voided on that basis. Some local authorities are calling for an investigation into the mis-selling of high-risk LOBOs, whilst Newham and Tower Hamlets councils are facing legal challenges from residents on this mis-selling and the negative consequences their populations are experiencing as a result.

Potential conflicts of interest have also been suggested in relation to the earning of commission from council LOBO deals by treasury management advisers (private sector companies which offer local authorities advice on their treasury management functions). The House of Commons Communities and Local Government Committee recommended in 2009-10 that the Financial Services Authority (FSA) take a more active role in the regulation of such advisers, with

[4] HM Treasury, Managing Public Money, section 5.9.1

legislative change necessary to ensure the effective regulation of these advisers

PWLB loans

Many of the arguments about local authority debt from LOBOs being 'illegitimate', 'odious' and 'unsustainable' also apply to debt from PWLB loans. In 2015-2016, the PWLB generated £2,931 million of interest income on its loans – this was an increase of £65 million on 2014[5]. In 2015-16, Scottish local authorities spent £933 million on repayments to the PWLB, and continue to owe a total principal sum[6] of £8,970 million[7].

PWLB rates are disproportionately low for Conservative-led councils. Some SNP, Labour and Liberal Democrat councils are paying comparatively higher interest rates on PWLB loans, and have subsequently turned to LOBOs for what can initially appear to be a 'better' deal.

Whilst local authorities' PWLB repayments represent HM Treasury revenue, local authority budgets have significantly contracted and continue to be exposed to further cuts – servicing debt to HM Treasury represents a significant additional hidden cost on local government. In this context, an amnesty on interest repayments – as called for by Kezia Dugdale at a recent Unite conference – or an amnesty on all pre-devolution debt – as called for by Unite Scotland – is welcome, but does not go far enough.

UNISON have argued that the Local Authority (Capital Finance and Accounting) (Scotland) Regulations 2016 offer the Scottish government the opportunity to relax the repayment of PWLB loans fund regulations, and provide 'flexibility in new borrowing or refinancing/restructuring existing borrowing which could potentially free up significant sums at a time of austerity cuts'. UNISON say that 'this could save upwards of £50 million'.

Improved governance and a Scottish PWLB

Improved governance, benchmarking and oversight of financial decision making within councils are required. Without these in place, financial decisions which are not in the public interest run the risk of being repeated.

If these scrutiny issues are properly addressed, a Scottish government controlled Public Works Loan Board, and the control of lending rates which would accompany this, could offer greater stability and better value to local authority finances.

[5] UK Debt Management Office, Public Works Loan Board Annual Report and Accounts 2015-2016, p. 12
[6] Excluding interest repayments
[7] UK Debt Management Office, Public Works Loan Board Annual Report and Accounts 2015-2016, p. 14