

The Highland Council

27 October 2016

Agenda Item	11
Report No	HC/42/16

Pre-Budget Statement

Report by Director of Finance

Summary

The purpose of this report is to provide an update on the current budget position, outline the financial impact of various modelling assumptions, assess options for a Council Tax increase for 2017/18, and to highlight the impact of Scottish Government policy decisions.

1. Background

- 1.1 The Highland Council, at its meeting on 25 February 2016, agreed a Revenue Budget for 2016/17 and noted an initial budget outlook for 2017/18 and 2018/19.
- 1.2 The Council, at an earlier budget meeting on 18 December 2014, has agreed specific budget proposals that include the financial years 2017/18 and 2018/19 as part of a 4 year Transformation Savings Programme. Updates on this Programme have been reported to each meeting of the Resources Committee.
- 1.3 At its meeting on 25 February 2016 the Council agreed an extensive list of savings proposals for 2016/17. Some of these proposals cover financial year 2017/18, particularly in relation to the Care & Learning Service, where savings have been identified against the school year rather than the financial year.
- 1.4 As always, budgets contain a number of assumptions which require to be reviewed regularly. This work has commenced for next financial year and the two following years, and this report provides an update on this work as well as forecasts about the level of grant reduction that the Council may expect.

2. Financial Environment

- 2.1 The Scottish Government has announced a delay in its own Spending Review to await the results of the UK Government's Autumn Statement (Spending Review), which will be announced on the 23 November. After this there is a significant amount of work required to clarify tax revenues following the devolvement of various additional tax powers to Scotland.
- 2.2 The Scottish Government has also indicated that, due to the level of uncertainty over tax and grant funding, it will only announce a one year budget for 2017/18. This announcement is planned for 15 December and Councils should receive notification of their grant on the same day (as was the case in 2015).
- 2.3 Members will be aware, from the Audit Scotland Overview Report on Local Government, of a strong reference to the need for medium and long term financial planning. Such planning will continue to be extremely difficult in an

environment of annual grant announcements, particularly given the significant proportion of Council funding (c83%) that is provided by the Scottish Government. However this places even greater importance on the need for the Council to plan ahead and produce longer term financial plans. The basis of this report therefore advocates the need for a minimum three year budget to model and assess the implications of future funding levels, and to provide guidance to services to enable service delivery options to be prepared.

2.4 The degree of uncertainty over the level of funding for local government is unprecedented. In terms of the overall Scottish Budget, the Scottish Government has indicated that its policy priorities are to:-

- Provide a cash uplift in excess of inflation to support the NHS
- Support and maintain police numbers
- Support and increase funding to devolved social security powers
- Maintain the basic rate of tax allowance

All of these specific factors suggest that the funding available for Local Government will continue to be squeezed and further real cash reductions in grant can be anticipated. In addition informal advice has been received to indicate that the Scottish Government will continue to require councils to maintain teacher numbers, thus ring fencing a significant proportion of the Council's overall budget.

2.5 Although no decisions have been taken, the anticipation is that Local Government can expect a grant settlement in line with that for 2015/16. This would suggest that the Council could see its grant reduced, in cash terms, by a further 4%. This situation is expected to continue over the next few years. In this scenario of recurring real reductions in funding the Council needs to consider options for reducing and/or stopping services to reflect the real impact of these grant reductions.

2.6 The scale of uncertainty, and the potential for significant funding cuts, means that the Council will require to address the situation and provide options for budget savings in a very short timescale if a balanced budget for 2017/18 is to be achieved. The situation is exacerbated if the Scottish Government continues to ring fence funding, or insist that certain outcomes are achieved, as was the case for 2016/17 where the Council faced significant financial penalty of £18m if it failed to comply with any aspect of the Government's demands. Such requirements mean that there may be certain budget lines, particularly in relation to Education and Social Care, where budget savings cannot be achieved. This will mean that reductions in other budgets will require to be much higher.

2.7 Within this financial environment the Council is, quite rightly, focussing on Service re-design as a way of prioritising budget expenditure and identifying ways in which services can be prioritised and delivered in the most effective way possible. The Council also needs to consider a more commercial approach and identify ways in which additional income can be generated in addition to reducing expenditure in various areas. Savings options will also have to be considered for service areas not currently planned for review under the work of the Re-Design Board.

2.8 The Administration Budget Team will have a key role to play in developing a budget strategy and leading officers to determine budget savings options for the Council to consider in due course. It is expected that proposals to balance the budget for 2017/18 will be presented, with the situation for future years being less formalised. This continues the practice over several years where the Council has agreed a firm balanced budget for “Year 1” with indicative budgets for future years.

3. Scenario Planning

3.1 Officers are undertaking financial modelling based on a number of different scenarios for the level of grant funding received from the Scottish Government. Given the indications about the funding for 2017-18 only a 4% scenario has been modelled for that year. Subsequent years have been modelled on a range of different scenarios ranging from 4% to 0% over these years.

3.2 Every 1% reduction in grant equates to approximately £4.4m less funding so alternative scenarios can easily be modelled if required.

3.3 Appendix 1 identifies a variety of scenarios for the period 2017/19 to 2019/20. These different scenarios require a number of high level assumptions to be made, both around budget pressures and council tax revenues.

3.4 Budget pressures reflect such things as inflationary increases in contracts, pay and pension uplifts, additional costs as a result of legislation or an inability to deliver savings approved in a previous year. A firmer figure of £14.039m for 2017-18 has been estimated with an assumed £10m in subsequent years.

3.5 In 2017/18 the Council Tax freeze is being ended with councils allowed to increase Council Tax by up to 3% without suffering any financial penalty. For the sake of the modelling it has been assumed that Highland will increase its Council Tax by 3% annually. Should the Council choose not to increase Council Tax at all over the three year period this would add a further £21.7m to the budget gap.

3.6 As outlined in section 2 it is not possible to say with any certainty which, if any, of the scenarios will come to pass but it would not be unreasonable to assume that anywhere between **£47m to £72m** of savings will need to be delivered over the next three years. This range could increase to **£69m to £93m** should Council Tax be maintained at its current level.

4. Impact on Council Services

4.1 As outlined in section 2.6 it will not be possible to allocate the savings requirement equally across all of the Council's services and activities. Some area will be 'protected' meaning that proportionally other areas would see a larger savings requirement.

4.2 If the Council faces a grant funding reduction of 4% in 2017/18, then 3% in 2018/19 and 2% in 2019/20 the estimated budget gap over that period is just under £60m. This equates to around 10.7% of the current revenue budget.

4.3 If schools are only able to deliver an annual budget saving of 1%, our partners NHS Highland and HighLife Highland deliver savings in line with the Council's

overall funding reduction, and other areas such as loans charges, ICT services, PPP and school transport only able to deliver limited, or no savings then the requirement for savings from other service areas increases considerably.

- 4.4 In the scenario outlined 'unprotected' services would have to deliver a 23% reduction on their current budget over the three year period, with a 10% saving required in 2017/18 alone.
- 4.5 In reality however some services areas may not be able to achieve a 23% saving so some areas may require to make an even higher saving. Savings requirements of this level may inevitably mean that significant service reductions, or complete withdrawal of some services, may be required.

5. Revenue Budget

- 5.1 The Table below shows the main constituent elements of a modelled budget for 2017/18 taking into account a range of planning assumptions that are described in the following paragraphs.

	£m
Roll Forward Budget	555.731
Budget pressures	14.039
	569.770
Funding:-	
Council Tax	118.428
Scottish Government Grant (4% reduction on 2016/17)	421.828
	540.256
Funding Gap	29.514
Less Previous Agreed Savings	<u>8.018</u>
	21.496
Less Council Tax increase of 3%	<u>3.500</u>
Residual Funding Gap	17.996

- 5.2 If the Council receives a 4% reduction in grant funding in 2017/18 this would mean an estimated budget gap of **£29.514m**.
- 5.3 The Scottish Government has stated that it will lift the Council Tax Freeze, but will place a 3% ceiling on any increase in Council Tax that councils may wish to make. In a Highland context a 3% increase in Council Tax will achieve an additional £3.5m in 2017/18. This has been assumed for planning purposes, but clearly this will be a decision for the Council in due course.
- 5.4 Section 1.2 of this report refers to budget savings for 2017/18 approved in prior years' budget rounds. These savings amount to £8.018m which would further close the budget gap to £17.996m.
- 5.5 Officers are currently reviewing these savings to ensure their full deliverability in 2017/18. Any that cannot be delivered or can only be partially delivered will

put the budget gap back up.

- 5.6 The budget gap for 2017/18 is predicated on budget pressures of £14.039m which require to be funded. More detail on this figure is provided at Appendix 2. The elements of this figure are also under review by officers and services have been asked to consider whether they have any other budget pressures, not currently accounted for in this figure, for which they require funding. Should the total budget pressures figure vary from the £14.039m figure the budget gap will move accordingly.
- 5.7 Should the savings and pressures figures hold firm then a residual budget gap of £18m would need to be addressed for 2017/18. The scenarios outlined in section 3 of this report would suggest that Members may not wish to consider the savings requirement for 2017/18 in isolation from subsequent years and look at how strategic change can deliver any potential savings required over the coming years.
- 5.8 Whilst it is not possible to say with certainty what the absolute level of savings to be delivered is, it is fair to say that the expectation is that it will be substantial. Following on from previous budget rounds it would seem as though the traditional method of budgeting and planning is no longer appropriate for the current time.
- 5.9 Members may have concerns about making excess budget savings in any year and reducing expenditure more than is required. Should that happen it would be an advantageous way to build up the Council's reserves which, at 2% of the annual revenue budget, are at historically low levels.

6. Council Tax Multiplier

- 6.1 As the Council is aware, the Scottish Government has proposed changes to the Council Tax multiplier. These changes will apply to properties in Bands E to H. Bands A to D are unaltered. The impact of these proposals is significant and will affect about 27% of all properties within Highland.
- 6.2 The Government expects to raise £100m across Scotland and to redistribute this sum directly to schools on the basis of number of free school meals provided by each school to improve educational attainment. These proposals represent a significant change to the principle of council tax being determined locally and spent on local services.
- 6.3 It is anticipated that the changes to the Council Tax multiplier will raise approximately £5m in Highland which will be deducted from the Council's grant settlement in anticipation of the Council raising the additional sum. The redistribution to schools is calculated to be in the region of £4m, which means a net outflow resource of £1m from Highland towards other areas of Scotland.
- 6.4 The Council is however asked to note that officers are aware of an alternative method of distribution that the Scottish Government is considering which relates to other measures of deprivation. Should this method be chosen, then the Council is only expected to receive £2.6m, a significant reduction and a net outflow of resource of £2.4m rather than "only" £1m.
- 6.5 The sum of £2.6m to £4m returned to Highland will be out with the Grant

Settlement. Whilst details are awaited it is anticipated that this will be paid as specific grant, directly to schools, and will have targeted outcomes. This amount cannot therefore be considered as forming part of the Council's budget considerations. At present the basis of allocation of funding is being challenged, and an alternative basis of distribution may have a different financial outcome for the Council.

- 6.6 One of the main issues for the Council to consider is the public perception of the changes and responsibility. Appendix 3 shows the impact of the change, distinguishing between a 3% increase that is within the Council's control, and the impact of the multiplier. On its own the multiplier creates a tax increase ranging from 7.2% at Band E to 22.5% at Band H.
- 6.7 The Government is also proposing changes to the Council Tax Reduction Scheme. There are taxpayers in Bands E to H that will qualify for financial support and this will come at an additional cost. Work is ongoing to quantify this at present, but the expectation is that additional costs will be fully funded by the Scottish Government.
- 6.8 Changes will be required to computer software to effect the multiplier changes. If applied to all charges these changes are not felt to be material. However the Scottish Government's strategy for Water & Sewerage charges which are billed with Council Tax on behalf of Scottish Water have just been clarified, and the Minister for Local Government has stated that the multiplier will not apply for Water & Sewerage charges. If the same multiplier does not apply then there will be significant logistical challenges of duplicate billing and additional costs, which may challenge the Council's ability to meet a 1 March 2017 billing deadline. These challenges will be common to all councils. There may also be an increased challenge to collect the tax as some taxpayers will face significant increases.
- 6.9 The Government's proposals however do go a small way towards making Council Tax a more progressive tax. It makes a broad assumption that links property value to wealth, and requires taxpayers in higher valued properties to contribute more to national tax.

7. Implications

- 7.1 There are no additional resource implications other than those highlighted in the report. There are no specific legal issues that require to be highlighted.
- 7.2 Risks – there are some significant risks around financial planning assumptions and the deliverability of previously agreed savings, any of which will impact on existing forecasts. The added uncertainty in the financial markets due to Brexit has not yet been factored in to any budget planning assumptions.
- 7.3 Equalities - The Scottish Government proposals seek to make Council Tax more progressive, seeking taxpayers to pay more tax when they live in higher value properties. There are changes proposed to the Council Tax Reduction Scheme which will seek to address ability to pay for taxpayers who are impacted by the changes.
- 7.4 There are no specific Gaelic, Rural, or Climate Change/Carbon Clever implications arising from this report.

Recommendations

Highland Council is asked to:-

1. Consider the financial risks highlighted in this report, and the implications of the level of uncertainty around the extent of grant cuts;
2. Consider the options for a Council Tax increase of up to 3%;
3. Note and consider the implications arising from the Scottish Government's proposed changes to the Council Tax multiplier as outlined in Section 4.

Designation: Director of Finance

Date: 17 October 2016

Author: Derek Yule

Background Papers: None

Highland Council- 3 year budget outlook.

Scenario 1- annual 4% reduction in SG funding

	17/18	18/19	19/20	
Roll forward budget	555.731	543.756	530.541	
Budget pressures	14.039	10.000	10.000	
	569.770	553.756	540.541	
Funding				
Council tax	121.928	125.586	129.353	assumes 3% annual increase
Grant funding	421.828	404.955	388.757	assumes year on year 4% reduction
	543.756	530.541	518.110	
3 year total savings requirement				
Budget gap to be met by savings	26.014	23.215	22.431	71.660

Scenario 2- 4%, then 3%, then 2% reduction in SG funding

	17/18	18/19	19/20	
Roll forward budget	555.731	543.756	534.759	
Budget pressures	14.039	10.000	10.000	
	569.770	553.756	544.759	
Funding				
Council tax	121.928	125.586	129.353	assumes 3% annual increase
Grant funding	421.828	409.173	400.990	assumes 4% reduction, then 3%, then 2%
	543.756	534.759	530.343	
3 year total savings requirement				
Budget gap to be met by savings	26.014	18.997	14.416	59.427

Scenario 3- 4%, then 2%, then 2% reduction in SG funding

	17/18	18/19	19/20	
Roll forward budget	555.731	543.756	538.977	
Budget pressures	14.039	10.000	10.000	
	569.770	553.756	548.977	
Funding				
Council tax	121.928	125.586	129.353	assumes 3% annual increase
Grant funding	421.828	413.391	405.123	assumes 4% reduction, then 2%, then 2%
	543.756	538.977	534.477	
3 year total savings requirement				
Budget gap to be met by savings	26.014	14.779	14.500	55.293

Scenario 4- 4%, then 2%, then 0% reduction in SG funding

	17/18	18/19	19/20	
Roll forward budget	555.731	543.756	538.977	
Budget pressures	14.039	10.000	10.000	
	569.770	553.756	548.977	
Funding				
Council tax	121.928	125.586	129.353	assumes 3% annual increase
Grant funding	421.828	413.391	413.391	assumes 4% reduction, then 2%, then 0%
	543.756	538.977	542.745	
3 year total savings requirement				
Budget gap to be met by savings	26.014	14.779	6.232	47.025

Budget pressures 2017/18**Appendix 2****£m**

Roll forward adjustments/full year effect

- 2nd homes council tax 2.600
- ICT contract extension 0.400

Provision for Pay inflation, pension increase and salary increments 4.823

Scottish Welfare Fund – grant funding change 0.219

Provision for contract inflation 2.329

Provision for known budget pressures

- Wick Schools (part year) 0.218
- Apprenticeship Levy 1.200

Treasury Management – Additional Borrowing Costs 2.250

14.039

Multiplier plus 3% Increase									Appendix 3
	Band A	Band B	Band C	Band D	Band E	Band F	Band G	Band H	Band@
2016/17	775.33	904.56	1033.78	1163.00	1421.44	1679.89	1938.33	2326.00	646.11
2017/18	798.59	931.70	1064.79	1197.89	1569.24	1952.56	2347.86	2934.83	665.49
Increase	23.26	27.14	31.01	34.89	147.80	272.67	409.53	608.83	19.38
% Increase	3.00%	3.00%	3.00%	3.00%	10.40%	16.23%	21.13%	26.18%	3.00%

Multiplier Only									
	Band A	Band B	Band C	Band D	Band E	Band F	Band G	Band H	Band@
2016/17	775.33	904.56	1033.78	1163.00	1421.44	1679.89	1938.33	2326.00	646.11
2017/18	775.33	904.56	1033.78	1163.00	1523.53	1895.69	2279.48	2849.35	646.11
Increase	0.00	0.00	0.00	0.00	102.09	215.80	341.15	523.35	0.00
% Increase	0.00%	0.00%	0.00%	0.00%	7.18%	12.85%	17.60%	22.50%	0.00%

Base report 11/08/2016

Band	Est % Increase Multiplier Only	No of Dwellings	DD Payers	Props with CTR
A	0.00%	19,603	9,862	6,639
B	0.00%	23,138	14,078	5,476
C	0.00%	23,472	16,006	3,696
D	0.00%	18,461	14,927	1,496
E	7.18%	18,176	15,447	818
F	12.85%	8,906	7,833	204
G	17.60%	4,336	3,807	53
H	22.50%	323	259	2
		116,415	82,219	18,384

Band	Est % Increase Multiplier Only	No of Dwellings	DD Payers as % of Band	Props with CTR as % of Band
A	0.00%	19,600	50.31%	33.87%
B	0.00%	23,115	60.84%	23.67%
C	0.00%	23,402	68.19%	15.75%
D	0.00%	18,396	80.86%	8.10%
E	7.18%	18,096	84.99%	4.50%
F	12.85%	8,869	87.95%	2.29%
G	17.60%	4,315	87.80%	1.22%
H	22.50%	323	80.19%	0.62%
		116,116		

Note: Of the 31,741 properties in Band E to H, 1,077 (3.4%) are in receipt of CTR

Band	Est % Increase 3% + Multiplier	No of Dwellings	DD Payers	Props with CTR
A	3.00%	19,603	9,862	6,639
B	3.00%	23,138	14,078	5,476
C	3.00%	23,472	16,006	3,696
D	3.00%	18,461	14,927	1,496
E	10.40%	18,176	15,447	818
F	16.23%	8,906	7,833	204
G	21.13%	4,336	3,807	53
H	26.18%	323	259	2
		116,415	82,219	18,384

Band	Est % Increase Multiplier Only	No of Dwellings	DD Payers as % of Band	Props with CTR as % of Band
A	3.00%	19,600	50.31%	33.87%
B	3.00%	23,115	60.84%	23.67%
C	3.00%	23,402	68.19%	15.75%
D	3.00%	18,396	80.86%	8.10%
E	10.40%	18,096	84.99%	4.50%
F	16.23%	8,869	87.95%	2.29%
G	21.13%	4,315	87.80%	1.22%
H	26.18%	323	80.19%	0.62%
		116,116		

Note: Of the 31,741 properties in Band E to H, 1,077 (3.4%) are in receipt of CTR

Mark Peden, Principal Support Officer,
Revenues and Business Support, 11/08/2016