

Agenda Item	13
Report No	HC/19/18

## HIGHLAND COUNCIL

**Committee:** Highland Council

**Date:** 28<sup>th</sup> June 2018

**Report Title:** Multi-Year Revenue Budget Planning 2019/20 to 2021/22

**Report By:** Director of Corporate Resources/Depute Chief Executive

### **1. Purpose/Executive Summary**

- 1.1 As part of prudent financial management this report looks ahead for the next 3 to 5 years considering the likely future funding and cost pressures the Council will face over the period. Given the high level of uncertainty around specific funding and cost issues a variety of different scenarios have been modelled to try to encompass all potential eventualities.
- 1.2 The scenarios modelled give rise to various 'budget gap' figures- an assessment of the gap between the cost of continuing to provide all Council services in their current shape and size, and the funding forecast to be available.
- 1.3 Any budget gap would need to be closed by spending less: by stopping and reducing services and delivering services more efficiently; and by increasing the level of income the Council generates from Council Tax and other fees and charges. All of these actions will be needed to balance the budget over the period 2019/20 to 2021/22.
- 1.4 Even in the most optimistic scenario modelled a budget gap of £34.1m is forecast over the three year period from 2019/20 to 2021/22. In the most pessimistic scenario a gap of £124.9m is forecast over the same period.
- 1.5 The report also provides a summary of the baseline budgeting work being done over the coming months to identify opportunities for meeting that budget gap with a view to agreeing a three year budget by February 2019.

### **2. Recommendations**

- 2.1 Members are asked to:
  - i. Consider the financial modelling assumptions
  - ii. Note the scale of the financial challenge facing the Council over the next three years with a potential funding gap of between £34.1m and £124.9m

- iii. Agree to prepare proposals for a multi-year budget for the period 2019/20 to 2021/22.

### **3. Wider Financial Context**

- 3.1 Members will undoubtedly be aware of the significant financial pressure that public sector finances have been placed under in recent years. In Scotland, local government has probably been the hardest hit of the wider public sector in terms of real terms reductions in funding.
- 3.2 There are many reports publicly available that illustrate the magnitude of those reductions, a recently produced report by SPICe highlights that between 2013/14 and 2017/18 there was a 7.1% fall in the local government revenue settlement in real terms. Over that same period the Scottish Government revenue budget decreased by 1.8% in real terms.
- 3.3 The same SPICe report identifies that over the period 2013/14 to 2018/19 Highland Council has seen a reduction in funding per head of population of £172, the fourth highest of all mainland authorities.
- 3.4 At the last Highland Council meeting members received Audit Scotland's report 'Local Government in Scotland, Challenges & Performance 2018' (see link in background papers section) which made similar points on funding along with a more detailed analysis on the difficulties facing local authorities.
- 3.5 To put some of those figures into a more local context, over the period 2013/14 to 2018/19 the Highland Council has had to approve budget savings of £102.1m as well as agree Council tax rises of 3% in each of the last two years in order to deliver a balanced budget.
- 3.6 The outlook for future funding settlements for local governments continues to look equally gloomy, albeit there is no certainty over what those funding levels will be. Section 4 below outlines some potential future scenarios that the Council may face.
- 3.7 Further evidence of the strain on the Council's budget can be seen in the financial performance for financial year 2017/18 where a deficit of £1.1m has been recorded. With Council general fund reserves at the exceptionally low level of £8.6 million the Council is particularly vulnerable to another year of overspend. A number of recurring budget pressures, challenging savings targets and risk of unforeseen events means the Council's budget is under a degree of pressure not seen for many years.
- 3.8 Recent years of single year budget setting have damaged the Council's financial resilience; decisions made have been expedient without linking in to a longer term financial or operational strategy. The budget setting process for the years ahead needs to be different, with Members being clear about their priority areas at the start of the process. Policy-led decisions must be taken for the medium term allowing a clear and ordered process for the rehabilitation of the Council's finances.

### **4. Scenario Planning**

- 4.1 As in previous years the Council has done a modelling exercise on its budget to estimate future spend and income scenarios. Spending scenarios are based on a continuation of services in their current form. None of these scenarios is intended to

give a definitive view on the exact funding gap that will face the Council in the coming years, rather it will give a range within which we are likely to find ourselves.

### **Income**

- 4.2 The Council has income from three primary sources, Government funding, Council tax and income from fees and charges. The Council has no control over the first of these, limited control over the second, and greater control over the third. From a budget planning perspective changes to government funding are included in the estimated budget gap figures. Potential extra income received from changes to fees, charges or Council tax are not built into the model as they are seen as ways of closing any potential budget gap.
- 4.3 The Scottish Government recently announced its medium term financial strategy and a link to that document is provided in the background papers section of this report. This document reiterates the Government's priority areas of Health, Police, Early Learning and Childcare, Attainment, Higher Education and Social Security which combined account for over 50% (and rising) of the overall Scottish budget.
- 4.4 An independent economic analysis of that strategy done for local authority Directors of Finance suggests that in the 'central' scenario put forward by government there will be no cash terms increase for core local government services over the next five years. In the 'lower' scenario a cash terms reduction of over 2% could be expected.
- 4.5 It should be noted that within the overall funding settlement for local government there will be variability between the actual level of funding change experienced by individual authorities. For that reason the Council's own modelling has identified three scenarios for future funding from government, namely 'flat cash', an annual 2% reduction and an annual 4% reduction. By way of reference a 1% funding reduction equates to around £4.4m.

### **Expenditure**

- 4.6 Salary costs accounted for just over £288m of Council spend in 2017/18, which is over half of overall net expenditure. There is currently significant upward pressure being applied to salary costs, via the Scottish government's pay policy, NHS pay policy and the demands of trade unions. Three different scenarios have been modelled for an annual pay award, increases of 1%, 3% and 5%.
- 4.7 A general provision of £7.5m annually has been allowed for non-staffing cost pressures. This figure is intended to cover contractual cost increases, inflationary cost increases, the additional revenue costs that may result from capital investment, the cost impact of demographic change and cost increases that may occur for any other reason.

### **Capital and Loans charges**

- 4.8 The Council agreed a five year capital programme in March 2018. That programme was predicated on it being affordable within the existing loans charges budget. For that reason all the scenarios modelled assume that the loans charges budget continues at its current level.

### **Reserves**

- 4.9 The Council's non-earmarked general fund reserve sits at £8.6m- around 1.6% of the annual revenue budget. The modelling has allowed for this to be increased by £1m annually with the aspiration that by the end of 2021/22 that reserve returns to in excess of the 2% level recommended as a minimum by Audit Scotland.

### Scenario outcomes

- 4.10 A summary of the outcomes from the scenario modelling can be seen in the table below. The budget gap figures reflect the total gap over the period from 2019/20 to 2021/22.

<b>3 YEAR BUDGET GAP 2019/20 - 2021/22 (£m)</b>
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Pay Award (per annum)	Grant Reduction (per annum)		
	0%	-2%	-4%
1%	£34.1m	£60.2m	£85.3m
3%	£53.5m	£79.6m	£104.7m
5%	£73.7m	£99.8m	£124.9m

- 4.12 Even in the very best case scenario modelled the Council would need to find savings or generate additional income totalling £34.1m over the period. An annual Council tax rise of 3% over the same period would meet around one third of a gap of that magnitude.
- 4.13 There are many variables that will influence the budget gap over the coming years and it is not possible to model each of them individually. The scenarios outlined will be regularly updated based on the best information available at the time but remain vulnerable to unexpected and significant changes in local and national economic data. Brexit, the level of inflation, government policy and borrowing rates are just some of the factors where an unexpected outcome could have a significant impact, either positive or negative, on the model.

### 5. 2018/19 budget process

- 5.1 In looking ahead to the process for agreeing a multi-year budget for 2019/20 to 2021/22 it is worthwhile reviewing the most recent budget process to see whether any lessons can be learned.
- 5.2 The 2018/19 budget process focussed on five themes, Redesign, Prioritisation, Efficiency, Income and Commercial and all these themes will be of relevance for any future budget process.
- 5.3 Areas where improvement could be made would be around consultation, most particularly with Members and the public. Any decisions made need to be clearly evidenced and articulated.
- 5.4 Most importantly any savings approved need to be robust, realistic and achievable. The Council is operating under increasing financial pressure as evidenced by the 2017/18 annual accounts which follow on this agenda. The Council has increasingly less scope to manage the non-delivery of savings or other unplanned events and Members must be prepared to take difficult decisions in order to meet their legal requirement to set a balanced budget.

## 6. Multi-year budget approach 2019/20 to 2021/22

- 6.1 It is becoming increasingly clear that any budgetary planning work done should look ahead more than one year to help manage the uncertainties ahead. The approval of a three year budget covering the period from 2019/20 to 2021/22 will form a key part of the Council's strategic planning process, tying in to the Council's programme and workforce plan.
- 6.2 Planning for the medium term will allow time for key strategic decisions to be taken, scrutinised and implemented. Many of the likely solutions to meeting the outlined budget challenge will require significant organisational change, impacting on our service users, staff and partners. Taking a budget approach that covers the next three years will enable us to properly manage, programme and resource that required change whilst giving us the flexibility to deal with any unforeseen eventualities.
- 6.3 The hardest part of any budget process comes in the identification of ways to meet the budget gap and, as in previous years, those can be split into broad thematic areas.
- The Council will seek to become more efficient, whether by redesign or other means, delivering services in as cost effective a way possible;
  - The Council will have to make tough choices, identifying its priority areas and stopping or reducing services in areas that are of lower importance;
  - The Council will need to become more commercial, identifying new income generating opportunities to make profit to support core services, or taking a considered approach to how it charges for services already provided.
- 6.4 Given the size of the modelled budget gaps it is highly unlikely that any one of these areas would provide sufficient savings, rather an approach that encompasses all areas will be required.
- 6.5 As a starting point of the baseline budgeting approach for identifying savings proposals it is necessary to develop our understanding of the different services the Council provides. Work is already underway within the Corporate Resources service to develop 'Service Profiles' for all areas of Council activity. A total of 40 areas have been identified and a list of those areas can be seen at **Appendix 1**.
- 6.6 The service profiles will consolidate all the relevant information we have available on each service, incorporating:
- A service overview;
  - An explanation of the current service delivery model;
  - Financial information- Prior year cost and income compared to budget, current year budget;
  - Performance information- Any local, national or other performance indicators covering cost, quality or satisfaction;
  - Staffing information- A profile of the workforce by job type and grade;
  - The assets or plant used to deliver the service, including a summary of any relevant items in the current capital programme;
  - A summary of any improvement activity currently underway or recently undertaken- this will include findings of any redesign, Lean and audit reviews; workforce planning, procurement, risk, commercial or other service-led improvement activity.
- 6.7 It is intended that service profiles are completed and agreed with services by the end of July 2018. The profiles will have three main users:

- Elected Members- who will use the profiles to deepen their understanding of services, consider their priority areas, and identify areas that might be targeted for improvement;
  - The wider public and other partners- in order that the public can begin to express their views on the services they value and understand the significant challenge facing the Council in balancing its budgets;
  - Council officers- who will use the profiles to identify further areas for improvement, working in partnership with the Corporate Resources service.
- 6.8 The service profiles will form the key baseline for all decision making with regard to the multi-year budget approach. It is very important that any decisions that are taken are evidence based, with a clear rationale. These profiles will therefore represent the base level from which any changes will take place, with individual savings/income proposals detailing the anticipated impact on service provision.
- 6.9 Once the profiles are produced work will be split into three different workstreams, essentially mirroring the groups referred to at 6.7 above. Work will be undertaken over the autumn to begin to develop proposals that will result in budget reductions over the next three year period.
- 6.10 As in previous years the Council will require to agree its budget at the February Council meeting. Should certain savings proposals be sufficiently advanced they can be considered at earlier meetings, for example that on the 13<sup>th</sup> December. Earlier agreement of savings would enable earlier delivery which may also benefit the current year's budget.

## **7. Implications**

- 7.1 Resource- This report outlines the financial resource pressures facing the Council over the coming years. That pressure will inevitably be felt by the Council's staff- the impact of which will be linked to the Council's workforce strategy. Delivering a multi-year budget will require significant input from managers and staff from across the organisation, supported by staff from all parts of the Corporate Resources service.
- 7.2 Legal- The Council has a legal requirement to set a balanced budget. The work as outlined in the report will enable the necessary decisions to be taken later this financial year.
- 7.3 Risk- The scenario modelling contained in the report carries a significant degree of associated risk. A large number of assumptions have been made about future conditions that may prevail, with different alternatives presented for those with the most significant impact. If reality differs markedly from any of the scenarios outlined the Council could find itself considerably better or worse off.
- 7.4 There are no Gaelic, Community (Equality, Poverty and Rural) or Climate Change / Carbon Clever implications arising as a direct result of this report.

Designation: Director of Corporate Resources/Depute Chief Executive

Date: 18<sup>th</sup> June 2018

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Background Papers:

SPICe report- <https://sp-bpr-en-prod-cdnep.azureedge.net/published/2018/5/21/Local-Government-Finance--facts-and-figures-2013-14-to-2018-19/SB%2018-34.pdf>

[https://highland.gov.uk/download/meetings/id/73565/item\\_11\\_audit\\_scotland\\_-\\_local\\_government\\_in\\_scotland\\_-\\_challenges\\_and\\_performance\\_2018](https://highland.gov.uk/download/meetings/id/73565/item_11_audit_scotland_-_local_government_in_scotland_-_challenges_and_performance_2018)

<http://www.gov.scot/Publications/2018/05/1497>

**List of Service Profiles**

**Appendix 1**

<b>Care and Learning</b>	<b>Chief Executive's Office</b>	<b>Community Services</b>	<b>Corporate Resources</b>	<b>Development and Infrastructure</b>
Additional Support Services	Chief Executive	Administration	Corporate Finance & Commercialism and Audit and Performance	Catering, Cleaning & Facilities Management
C&L Service Management and Resources	Legal Services	Amenity Services	Directorate and People	Director & Business Team
Childcare and Early Learning	Members	Car Parks	ICT Services	Environment & Economic Development
Children's Services	Policy & Reform	Environmental Health	Loan Charges	Housing Development & Private Sector Housing Grant
Commissioned Leisure Services (HighLife Highland)		Harbours and Ferries	Revenues and Customer Services	Infrastructure
Commissioned Adult Services (NHS Highland)		Lighting Services	Welfare	Investment Properties
Education- Centrally Funded		Housing- Non-Housing Revenue Account		Planning & Building Standards
Education- Devolved Schools		Roads		Property Asset Management
Other Culture, Sport and Leisure		Transport		Property
Services for Vulnerable Adults		Vehicle Maintenance Trading Account		
		Waste & Environmental		