Agenda Item	**11**
Report No	**HC/22/22**

THE HIGHLAND COUNCIL

Committee: **Highland Council**

Date: **22 September 2022**

Report Title: **Financial Crisis – Our Council and Our Communities**

Report By: **Chief Executive**

1. Purpose/Executive Summary

1.1 On 7 September 2022 the Deputy First Minister made a statement to the Scottish Parliament on public sector pay and emergency budget review, highlighting the significant challenges ahead for the public sector purse. The excerpt from the speech quoted below is unequivocal in the scale of the challenge ahead:

'*This is not just a cost of living crisis as some characterise it. The costs of doing business, the cost of third sector support and the cost of public services are all rising as well.*

Indeed, in all of my experience, now and during my previous tenure as Finance Secretary, there has never been a time of greater pressure on the public finances.'

This report provides Members with an update on how the Council's own finances are affected by the current financial crisis as well as those of our residents.

1.2 The Council is experiencing significant pressure on its finances, predominately driven by the current high-inflation environment. As reported to the Corporate Resources Committee earlier this month an overspend of £9.6m is forecast against the current year's revenue budget. A summary of that report is included in this report alongside reference to a number of risks that could adversely impact on that position with consequential impacts for future years.

1.3 This report looks ahead to 2023/24 and forecasts a budget gap of £40.9m for that year. Given wider economic uncertainty no absolute figure is provided for subsequent year budget gaps but the gaps are anticipated to be significant and of a similar magnitude to 2023/24 if high inflation persists.

1.4 To address the financial challenge a number of budget strategies are proposed- the implementation of which will help mitigate the forecast current year overspend as well as support the delivery of savings in future years. Those strategies focus on the Council's People Strategy; Increasing Income; Service Prioritisation and

Redesign; Asset Management, Contract Management, Capital Programme Review, and Reserves Review.

1.5 Given the financial challenges facing the Council which continue to emerge, our key fundamental principles in our People Strategy are underpinned by the direction of travel to meet these challenges. As we move from recovery and transition to a post-pandemic workplace, we need to reshape the organisation, by reducing our headcount through natural turnover, and reprioritising to build an agile and flexible workforce which is sustainable for the future. We need to shape and repurpose our workforce at pace while engaging with our staff and working with our trade union partners.

1.6 This report also sets out the current position regarding the review of the schools Devolved School Management (DSM) scheme and the review of Early Learning and Childcare (ELC) partner funding rates, with current arrangements to remain in place and the review activity to continue in light of the financial crisis facing the Council.

1.7 The cost of living crisis is affecting our residents with those on the lowest incomes being disproportionately impacted. Financial pressures within households can have far reaching effects including on physical and mental health, and relationships. This report contains proposals to help alleviate the cost-of-living crisis and to complement the support and interventions by the UK and Scottish Governments. These proposals are in addition to the £3.429m package of welfare support agreed by the Council in June 2022 which enabled payments for eligible households to be made during August 2022.

2. Recommendations

2.1 Members are invited to

Note:

i. Note the financial position for financial year 2022/23 and the forecast budget gap of £40.9m for 2023/24

ii. The content of the letter from the Cabinet Secretary for Finance and Economy regarding the Spending Review as set out in **Appendix 1** to this report.

iii. The Scottish Government's financial position with regard to the pay award as set out in the Depute First Minister's letter at **Appendix 2** to this report, which includes "All areas of the public sector will have to make challenging savings to live within existing budgets".

iv. That the current schools DSM scheme, and current ELC partner funding rate will apply, with work on reviewing both the DSM scheme and ELC partner rate to continue in light of the financial crisis facing the Council.

Agree:

i. Implement budget strategies as detailed in section 8 of this report;

ii. Allocate £3.223m from the Council's non-earmarked reserves to:

a. provide non-recurring cost of living support payments of £145 to each household in receipt of council tax reduction and specified council tax exemptions as set out in this report This will require £2.523m to be provided.

b. extend the existing Monday to Friday free school meal holiday payments to include weekend provision up to and including Easter 2023. This will require £0.200m to be provided.
c. provide grants to individual organisations of up to £10k for community-led initiatives. Non-recurring funding of £0.450m is to be provided.
d. provide non-recurring funding of £0.050m to FareShare to purchase food for distribution across the Highlands.

iii. That the Council collaborates with the Scottish Government with a view to engaging with utility companies to seek more preferential energy tariffs for social tenants.

iv. That a member workshop be held in October in order to consider future capital investment for council housing in more detail.

3. Implications

3.1 **Resource**: Resource requirements are set out in this report and if approved will commit non-recurring funding of £3.223m to be drawn from non-earmarked reserves.

3.1.1 The Council holds general reserves for two main purposes; for transformational investment and for the management of risk. The forecast overspend in the current financial year (2022/23) as described in this report would be met from the Council's non-earmarked general fund reserve, reducing it from its current level of £19.2m (3% of the annual revenue budget) to £9.6m (1.5% of the annual revenue budget).

3.1.2 If Members approve the proposals of £3.223m in today's report that would further reduce non-earmarked balances to £6.4m (1% of the revenue budget). A reserve at that level would sit below the Audit Scotland recommended range for this reserve of 2-4% of the annual revenue budget, and the Council's own target (3% of the annual revenue budget).

3.1.3 Any change in the forecast 2022/23 outturn position, either positive as a result of the budget strategies outlined in section 8 of this report, or negative as a result of further risks crystallising, would impact on the level of this reserve at year end.

3.1.4 The Council also holds a number of earmarked reserves, i.e. funds held for a specific purpose, including investment in transformation. Whilst these funds are not for the most part available for general use they form part of the Council's overall financial position. As reported to Corporate Resources Committee on the 8th September those funds currently stand at £87.7m with further drawdowns to take place to offset spend incurred during the course of 2022/23.

3.1.5 In a situation where the Council's non-earmarked reserve is exhausted, or significantly depleted, it would become necessary to review and potentially remove earmarked funds where possible to do so. This would mean reducing the level of funding for certain investment priorities. This review will be undertaken as part of the budget strategy covered in section 8 of this report.

3.1.6 The level of the general fund non-earmarked and earmarked reserves (those elements likely to be able to be repurposed) is anticipated to be sufficient in the short term to manage financial risks for 2022/23 and 2023/24, including the risk that insufficient savings are able to be delivered to fully meet the 2023/24 budget gap. A continuing high-inflation context may see these reserves reduced, limiting the ability to invest in transformation activity, provide any temporary support in addressing the 2024/25 budget gap, or manage financial risks from 2024/25.

3.2 **Community (Equality, Poverty and Rural)**: The proposed welfare package of support will help alleviate inequalities, poverty and disadvantage arising from the cost-of-living crisis.

3.3 **Legal:** The proposed spend aligns with the guiding principles and discretionary nature of local and flexible decision making.

3.4 **Risks:** These proposals alone will not fully mitigate the cost-of-living crisis for our communities. Some residents and families will need specialist support from the Council and our public sector partners, which may include emergency responses and crisis management. We will continue to collaborate with our community partners to enable resources to be targeted where they are most needed and will continue to maximise incomes for our residents through our Welfare Support and Citizens Advice services.

3.4.1 There are two different types of financial impact that may occur if risks crystallise. Some risks relate to one-off events that have an immediate financial impact that requires to be addressed. Once that risk is addressed there may be no further financial impact.

3.4.2 Other risks may have longer term financial impacts, i.e. they may have a recurring impact on the budget. Items of this nature can be mitigated through reserves in the year they occur, but recurring and lasting impacts will need to be factored into future years' budget processes as a budget pressure.

3.4.3 The holding of reserves to mitigate any risks therefore can only really offset the initial impact of a risk crystallising with long-term impacts needing to be managed through making equivalent savings elsewhere in the budget. Once reserves are depleted they too may need to be recovered, depending on residual risk levels.

3.4.5 From a financial perspective the single biggest risk that the Council faces is that of long-term financial sustainability. The holding of reserves can have only a minimal impact on this risk - reserves can mitigate a budget gap on a one-off basis only but cannot keep bridging a budget gap on a recurring basis. As such it is important that when reserves are used, they are used for investment to support sustainable, balanced budgets.

3.4.7 The key factor driving financial risk is inflation with the potential for significant cost increases in the short term. Those impacts may be seen across any area of the Council's spend. Whilst allowances for inflation were made in the 2022/23 budget impacts are coming through that are in excess of those anticipated.

3.4.8 It is also important to note other specific financial risks that may affect both the 2022/23 and future years' budget:

- 2022/23 Pay award - this has not yet been agreed with discussions with the different trade unions (SJC, Teaching, Nursing) at different stages. Any improved offer from that currently made will have a financial impact
- Non-pay cost inflation, eg contracts currently being reprocured are seeing significant cost increases.

- Demand led pressures such as social care, winter maintenance or adverse weather may see significant moves in cost forecast over the year from that currently forecast

3.5 **Climate Change/Carbon Clever**: Wherever possible, the Revenues & Business Support – Service Delivery team will engage electronically with those eligible for welfare payments. The Welfare Support team will continue to provide a telephone and email service where this is appropriate and continue to provide in-person services at various locations across the Highlands, including our Service Points.

3.6 **Gaelic:** There are no specific Gaelic implications directly arising from this report.

4. Financial Crisis

4.1 ***National***

On 7 September 2022 the Deputy First Minister made a statement to the Scottish Parliament on public sector pay and emergency budget review, highlighting the significant challenges ahead for the public sector purse. The full transcript of that statement can be seen via the link below:
https://www.gov.scot/publications/ministerial-statement-public-sector-pay-emergency-budget-review/

The excerpt from the speech quoted below is unequivocal in the scale of the challenge ahead:

'*This is not just a cost of living crisis as some characterise it. The costs of doing business, the cost of third sector support and the cost of public services are all rising as well.*

Indeed, in all of my experience, now and during my previous tenure as Finance Secretary, there has never been a time of greater pressure on the public finances.'

4.2 In short, highly uncertain economic times are resulting in an increasing cost of living with underlying factors such as energy and food cost rises impacting on individuals, families, communities, businesses and the public sector.

4.3 In this context the public sector is especially challenged, with increasing demands for services and a need to support those in need having to be balanced within a fixed resource allocation. Given the impact of inflation the spending power of those finite resources is becoming diminished.

4.4 This report aims to provide to Members with an overview of the wider context, the impact on the Council's short and medium-term finances, and potential interventions it may wish to make to support the most vulnerable in our communities.

5. Financial Context – Highland Council current year (2022/23) financial position

5.1 As reported to the Corporate Resources committee on 8 September 2022 as part of the 2022/23 Q1 revenue budget monitoring the Council is forecasting an overspend for the current year of £9.6m. This forecast overspend is caused by the following principal factors:

- The excess unbudgeted cost of the current pay offer made to staff (£5m)
- Net forecast overspend against service budgets, much of which relates to inflationary impacts (£3.6m)
- Unbudgeted utility cost pressures (£1m)
- Delayed delivery in asset management saving (£0.6m)
- Offsetting factors- Council tax income and unallocated budgets (-£0.6m)

5.2 The background papers section of this report provides a link to the report to the Corporate Resources committee which provides a more detailed explanation of all the factors that underpin this forecast position.

5.3 Inflation is seen as being the underlying factor to the majority of the forecast overspend, driving the Council's direct costs upwards and leading to a pay offer significantly in excess of the original budget provision made.

5.4 The latest pay offer made by COSLA to the trade unions contains a differentiated offer, with those at the bottom of the salary scales receiving an uplift of around 10%, reducing to an uplift of just under 3% for those at the top of the salary scale. The overall cost of this award is roughly estimated at around 6.1% of the total pay bill with funding provided as follows:

- Council budget pay provision (March 2021 budget): 2%
- Additional SG funding (August/September 2021): 2.6%
- Unbudgeted pressure on Council budget (as per 5.1 above): 1.5%

5.5 The risk section of this report covers a variety of factors that could impact on the financial position reported for 2022/23 (as well as future years) and reduce or increase the currently forecast variance. Any overspend that transpires at year end will require to be funded from the Council's reserves.

5.6 Officers are actively managing the in-year position and, where possible, endeavouring to ensure that all service budgets are at least balanced by the end of the financial year. Any work done to implement the budget strategies as described in this report is likely to help reduce spend in the current financial year, thereby reducing the forecast overspend further.

6. Budget outlook 2023/24

6.1 The factors underpinning the forecast 2022/23 outturn position are expected to perpetuate into 2023/24 and if inflation remains high it will contribute to a sizeable budget gap. The budget gap for 2023/24 will be doubly affected by such factors, firstly providing sustainable funding for the 2022/23 cost pressures on a recurring basis, and secondly by needing to mitigate the 2023/24 impact of such factors.

6.2 There are three main factors that contribute to any budget gap which are:

- Increasing pay costs
- Non-pay cost increases/inflation
- Changes in core grant funding from government

More detail is provided on those items in the sections below with a summary provided in the following table. It is important to note that given the highly uncertain environment a high degree of caution needs to be exercised around these figures.

Summary of potential budget gap 2023/24	
Element	**£m**
Pay- unfunded element of 22/23 award	5.0
Pay- 23/24 pay award (assumed at 3.5%) and increments	15.9
Non-pay cost increases	20.0
Change in core revenue funding	0.0
Total budget gap 23/24	**40.9**

6.3 The potential budget gap of £40.9m for 2023/24 reflects the mismatch between anticipated costs and income if the Council is to deliver the same services in the same manner as 22/23. In short it would cost £40.9m more to deliver services than the income the Council expects to receive.

6.4 As Councils have a legal requirement to deliver a balanced budget the budget gap would need to be alleviated by:

- Reducing expenditure (i.e. making budget savings)
- Increasing income from controllable sources (i.e. fees and Council Tax)
- Using reserves

It is important to note that any use of reserves to balance the budget is a temporary measure only and will mean a sustainable solution will need to be found the following year for recurring costs.

6.5 The pay elements in the table at 6.2 are highly uncertain at the current time. The costs relating to 2022/23 reflect the current pay offer and as such reflect a best-case scenario. Should any union reject the offer and a higher offer is made that requires Council funding (as opposed to additional funding from government) the gap would widen. The assumption made for the 23/24 pay award replicates the cost to the Council of the 22/23 award (i.e. 3.5% of the pay bill). It is unclear if any additional government funding will come for the 23/24 pay award - if it does not and inflation remains high there may be significant upwards pressure on this sum. An allowance has also been made in this figure for incremental pay progression as staff move upwards through the pay points. A recessionary environment may see less staff turnover, leading to a net overall upwards movement across spinal pay points for the current staffing compliment.

6.6 The non-pay cost increases figure of £20m reflects a high-level estimate of what these pressures might be in 2023/24. For reference the equivalent figure in the 2022/23 budget was £18.4m where arguably the impact of inflation was only just beginning to emerge. At this stage specific figures have not been put against specific individual items, but all of the items listed below are expected to be sizeable budget pressures for 2023/24:

- Increased cost of bus contracts (more information elsewhere on this Council agenda)
- Utility cost increases
- Increased costs relating to care home provision (more information elsewhere on this Council agenda)
- Rising interest rates leading to increased loans charges
- Indexation clauses on existing contracts (e.g. PPP/PFI)
- General cost increases (e.g. food, vehicle fuel)
- Increased rates of taxation (e.g. landfill tax, business rates)

- Revenue consequences of capital investment (running and operating costs associated with new buildings/facilities)
- Recurring Covid budget pressures from 2022/23 (these pressures were funded from reserves on a one off basis in 2022/23)
- Any recurring and unmitigated 2022/23 budget pressures (contributing to current forecast overspend)

6.7 The forecast position in respect of revenue grant funding from the Scottish Government is for a 'flat cash' position. This means that the Council is expecting to get the same amount of general revenue grant funding in cash terms in 2023/24 as it is receiving in 2022/23. In a high inflationary environment that flat cash level of funding will equate to less spending power year-on-year as all costs increase. The flat cash position echoes the Scottish Government's Resource Spending review published in May of this year: https://www.gov.scot/publications/scottish-resource-spending-review/#:~:text=The%20Resource%20Spending%20Review%20is,focused%20on%20delivering%20our%20outcomes. **Appendix 1** to this report contains the letter from the Cabinet Secretary for Finance and Economy setting out the Scottish Government's Resource Spending Review.

6.8 As with the assumptions around pay and non-pay cost inflation there is significant uncertainty around this assumption about funding. Much has changed since the Resource Spending review was published in May and the Scottish Government is currently reassessing its spending priorities. This may lead to less funding being available to local authorities. Additionally, a flat cash settlement for the local government sector may see some councils receive a cash uplift and others a cash reduction within that overall funding envelope. Finally, it is unclear whether the councils will be asked to deliver any additional or enhanced services (with associated cost) from within that flat cash envelope. **Appendix 2** to this report contains the letter from the Deputy First Minister and Cabinet Secretary for Covid Recovery regarding the 2022-23 Scottish Budget.

6.9 At this stage no changes in the level of Council Tax income receivable have been factored into the budget gap calculations. The overall impact of Council Tax on the budget gap will depend on:

- Council Tax rates for 2023/24
- Any change in the Council Tax base (i.e. the number of properties)
- Any change in collection rates/bad debt provision

For reference a 1% increase in the rate of Council Tax will equate to roughly £1.3m of additional income to the Council.

7. Budget outlook- medium term

7.1 The CIPFA Financial Management code is clear that medium to long-term financial management must be a key consideration of all those responsible for a local authority's finances. Given the heightened level of uncertainty around both the 2022/23 and 2023/24 financial outlook it is considered that setting out scenarios for the anticipated budget gap over the next five years would provide so wide a range as to any potential budget gap that it would not effectively support long term operational planning.

7.2 To give Members some idea of the potential budget gaps the Council might face in future years it is worth noting that historically annual budget gaps have been:

- An annual gap of £40m in 'exceptional' years (2015/16 and potentially 2023/24)
- An average gap of £15m - £20m in 'normal' years.

As outlined in previous sections of this report the significant uncertainty, particularly around the magnitude of the impact of inflation and how long the current heightened inflation will last mean that the current context is quite different from those seen historically when inflation was relatively low. Exceptional years in future may see annual budget gaps higher than those ever previously experienced.

7.3 In terms of the key variables that affect the budget gap an illustration of the impact of potential changes is provided below:

- A 1% annual change in the pay assumption will have an average +/- £3.8m annual impact or a +/-£19m impact over the five year period
- A 1% change in the government funding assumption will have a +/- £5.2m annual impact or a +/-£20.8m impact over the period 2023/24 to 2026/27

As per the 2021/22 annual accounts the Council had over £390m of non-staffing costs (excluding financing costs). Many costs in this area may be directly impacted by inflation.

7.4 Based on the figures above, over a 'normal' 5-year period the Council might expect to have to deliver £75m to £100m of budget savings or additional income generation in order to balance its budget. Current circumstances suggest the gap for the next 5 years could be significantly higher, so large that a fundamental reassessment of the role of the Council in providing public services, and its capacity to do so, is required.

7.5 Despite this uncertainty and the magnitude of the short term (2022/23 and 2023/24) challenge it is essential that the Council does not lose sight of the transformational changes needed to secure the Council's medium-term financial sustainability.

8. Budget strategies

8.1 Given the scale of the challenge facing the Council it is essential that a number of strategies to reduce spending are put in place now, to help mitigate both the forecast overspend in the current financial year and support the development and delivery of budget savings into 2023/24. The sections below introduce the strategies which will be implemented immediately.

The scale of the challenge facing the Council will mean that these strategies will need to be implemented at pace and within timelines the Council has not historically worked to. Such pace may mean compressed opportunity for staff and stakeholder engagement or consultation or deliver unanticipated impacts.

8.2 **People Strategy- reduce, reshape, reprioritise**

The Scottish Government's Resource Spending Review outlined '*A pathway to return the overall size of the public sector workforce broadly to pre-pandemic levels, while supporting expansion in key areas of service delivery, helping to hold total pay bill costs, as opposed to pay levels, at 2022/23 levels'.*

Whilst recent public statements from the Scottish Government may suggest that even further workforce contraction is required the Council will inevitably need to echo the Scottish Government approach and hold total pay bill costs steady.

The Council will, where possible, continue to have a no redundancy policy, and focus on natural turn over within the organisation to reduce the head count. It is important that jobs are protected retain key skills retained while reducing, reshaping and reprioritising the work we do. Current and future vacancies will be reviewed as they arise to ensure the Council has the right skills and staffing resource levels to deliver services that meet the changing needs of our communities. Fixed term contracts will not be used as a tool for flexibility. The flexibility of staff will come from the design of job roles and inherent behaviours required from our workforce who in turn will benefit from secure employment, fair work and pay with prospects to develop.

8.3 **Increasing income**

Whilst the majority of funding the Council receives comes from either grants from Government or Council Tax, the Council still raises substantial sums locally through fees and charges. This element of the strategy will look at optimising existing income streams including whether any in-year adjustments to charges are needed.

New opportunities for charging will also be considered including whether any services currently provided free of charge can or should have charges introduced. New areas of income generation will be considered, including the provision of new or additional services, however it is essential that the cost of providing those services is taken into account to ensure that income received is in excess of the cost of providing the service (i.e. it is profit-making). For any potential opportunity a robust business case will be required to understand potential benefits and risks.

The Council also needs to decide on whether it wishes to take advantage of new or forthcoming opportunities for income generation, whether that be from a Workplace Parking Levy or a Transient Visitor Levy (the introduction of the latter is included in the Scottish Government's programme for government)

8.4 **Service prioritisation and redesign**

The Corporate Resources Committee of 8 September approved the Council's ICT Strategy, Digital Transformation Strategy and Information and Data Strategy and a Business Intelligence Strategy follows on today's agenda. These key strategic pieces provide the framework for the effective redesign of Council services to allow alignment with the Council's priorities. The Council will use data to understand its current performance and costs and use existing governance structures and processes, such as Lean reviews and the Redesign Board to effect redesign.

A demand management approach will be introduced to help the Council understand why its services are used and to help support redesign activity. Demand is split into five categories, with different considerations for how each type is best managed. Those demands are:

- Failure demand- Is demand rising as a result of public service failure or poor service design?
- Avoidable demand- Is demand arising from particular behaviours that could be influenced or changed?

- Excess demand- Is the Council providing more than is needed, or inadvertently creating demand through dependency?
- Co-dependent demand- To what extent is demand unintentionally reinforced and entrenched by service dependence?
- Preventable demand- To what extent is demand arising from causes which could have been addressed earlier?

In alignment with the development of the Council Programme the final part of this strategy element will relate to service prioritisation and making difficult decisions that certain existing services no longer continue to be priorities for the Council. Where services are no longer viewed as priorities the reality of the financial situation is that those services will need to be reduced substantially or removed in their entirety.

Aligned to this local service prioritisation activity COSLA and the Scottish Government are working together to understand which areas of Council service provision reflect national priorities. For those areas which are not national priorities joint discussion will be needed on whether ring-fencing can be removed from certain funding streams, allowing local determination on spend, or whether statutory requirements around service provision or spending can be amended to allow for resources to be reprioritised.

8.5 **Asset management**

The Council has clearly stated its ambitions in regard to its approach to asset management but a more dynamic delivery of the approach is required. Urgent steps need to be taken to reduce the Council's asset base at pace, with consideration given to mothballing certain properties at short notice and prior to the winter heating season. Disposal or demolition of properties will yield larger savings but the timeframe to dispose or demolish properties will be longer and likely impact on the 2023/24 budget gap.

This approach will be taken through the Council's redesign board to support fast-paced delivery with staff currently working in affected properties co-producing alternative working solutions that work for both them and the wider organisation.

Tying into asset rationalisation a concerted effort to reducing the Council's energy usage will be required. Whilst the closure of a building will yield savings the Council must reduce its energy consumption in those buildings that remain open. Behavioural change will be key to the delivery of that approach with all staff requiring to take the same responsibility for their share of the Council's energy usage as they do for their own domestic usage.

Other elements of this strategy will include larger projects such as depot rationalisation and working across all public sector partners in specific geographies to deliver co-location.

8.6 **Contract management**

Previous sections of this report have highlighted the substantial levels of non-staffing spend incurred by the Council and the risk posed to this spend by inflation. A different approach will need to be taken with all contracting parties to make them aware of the Council's financial challenge and that the Council will only in very exceptional circumstances consider any increases to contract values.

Contractors and partners will be asked to work collaboratively with the Council to look at if services can be improved within existing or reduced contract values with the understanding that the current cost of contracts is the absolute maximum affordability envelope for that contract.

The Council will collaborate with contractors and partners to understand where cost reductions can be made, linking in to other elements of this proposed budget strategy. This may mean changes in ways of working, reducing any areas of duplication of service provision, generating income or reducing and reshaping service provision.

8.7 **Capital programme review**

In June 2022, Members acknowledged the need to review the capital programme given the inflationary cost increases being seen in projects across the programme. Review work is already ongoing to look at revisions to project costs, scope and timing.

Where it was previously acknowledged that some projects might have to be removed from the programme, reduced in scope, or deferred in order to meet cost pressures on other projects it is now the case that the overall funding envelope for capital investment will have to be reviewed. Significant increases in interest rates will mean the Council will have to spend more of its loans charges budget in financing debt, reducing the amount available to fund actual capital investment.

Given the revenue budget challenge no area of the revenue budget should be exempt from review for potential budget savings. Should the Council wish to make savings in its loans charges budget then further contraction of the capital programme will be required.

In the interim period until the capital programme review is complete it is intended that all contract awards with a value greater than £1m will be subject to review from the officer Capital Programme Board to determine whether any deferral in contractual commitment is possible.

8.8 **Reserves review**

As described earlier in this report the Council has substantial earmarked reserves- i.e. funds held for a specific purpose. Some of these reserves are held for specific statutory or legal reasons, some reflect specific external funding streams received, and others reflect priority spending commitments previously made by the Council.

Given the changing financial outlook a review of all of these reserves will take place to determine whether any could be reprioritised if required. Any funds that can be reprioritised may be required to bolster the Council’s non-earmarked reserve to help mitigate future financial risks including supporting the 2023/24 budget gap.

Pending completion of the review it is intended that no further contractual commitments (e.g. employing additional staff or signing contracts for goods or services) will be made unless time critical.

It is important to note that this approach would only bring a one-off benefit- any reserves freed up by this approach can only be spent once. As such this element of the strategy does not offer a recurring solution to the budget challenge, but merely buys time or opportunity until recurring budget savings are found.

9. Devolved School Management (DSM) Scheme Review

9.1 New Devolved School Management (DSM) Guidelines on school funding decisions for Local Authorities were published in June 2019. These were jointly produced between Scottish Government and COSLA, and form part of the current Education Reform Programme. This guidance was issued by Scottish Ministers under section 13 of the Standards in Scotland's Schools etc Act 2000.

9.2 Scottish Government expectations, revised due to the Covid-19 impact, were that revised DSM schemes, having undergone review and consultation, would be agreed and implemented by August 2022. The Council has been working on its DSM scheme review, with input from Head Teacher and Trade Union representatives through a DSM review Working Group, and with the intent of final recommendations being considered by members this Autumn.

9.3 In light of the financial crisis and the context set out within this report, it is not appropriate for the Council to be asked to make what would be recurring and longer-term financial commitments, in the form of a revised DSM scheme at this time. The purpose of this section of the report is to ensure that elected members, and in turn wider stakeholder interests, are aware of the position, and the reasoning behind this position.

9.4 Decisions relating to the DSM scheme, cannot be made independent of the wider financial crisis and context facing the Council, and as such will need more time and consideration as part of the Council's financial planning going forward. This matter will be considered further, in future reports to Council.

9.5 Members should be assured that the existing DSM scheme and supporting documentation remains in place, as it has been in recent years, and our Highland schools already have the clarity in relation to their current budget as they returned to start the new year in August. In turn, the staff resources deployed in our schools from August do reflect the use of additional Scottish Government resource in the current year to support our schools, their recovery and the delivering of learning and teaching. The deferral of a decision on the DSM scheme review will have no direct impact in relation to the staff deployed into our schools for the current session.

9.6 While the assurance above is given in relation to the consequence of deferring a DSM scheme review decision, this is not intended to signify that the Education budget or the DSM budgets devolved to schools are somehow protected or exempt from the wider financial crisis. As decisions and actions are taken forward as part of the Council's response to the financial crisis, it is expected that implications for school budgets are considered as part of that process.

10. Early Learning and Childcare (ELC) Partner Sustainable Rate Review

10.1 Funded ELC of 1140 hours per annum, is delivered across the Highlands through a combination of Council settings, partner and childminder provision. The Council has circa 51 funded ELC partner providers plus 28 Commissioned Childminders, and an annual budget of £7.5m for payments to these providers.

10.2 Scottish Government issued guidance relating to 'Partner Sustainable Rates' as part of their wider 'Funding Follows the Child' policy framework for ELC. That guidance had an expectation that Scottish Councils would review the funding rates paid to ELC providers and using the guidance document as a framework. The expectation was that the outcome of that review, and revised funding rates would be effective August 2022.

10.3 Some of the key principles set out within the Scottish Government guidance are as follows:-

- the rate paid to funded providers should be sustainable and affordable by the Local Authority whilst meeting the following:-
    - to support delivery of a high quality ELC experience for all children.
    - a rate that reflects the cost of delivery, including the delivery of national policy objectives.
    - allow for investment in the setting – staff, resources and physical environment.
    - enable payment of the real Living Wage for those childcare workers delivering the funded entitlement

10.4 The Council had been working with a small working group of partner representatives, and reviewing data output from a national survey of partners, led by the Improvement Service, to inform the review.

10.5 In November 2021, the Education Committee agreed to an interim uplift in the hourly rate of funded ELC from £5.31 to £5.43 (a 2.3% increase) effective August 2021. This was in recognition of the pay and inflationary pressures faced by providers at that time, and with the review not at that stage concluded. This was with an expectation that a final review outcome would be reported to members this Autumn, to formally conclude the review and the funding rate to apply from August 2022 onwards.

10.6 As set out within this report, the financial crisis facing the Council has entirely changed the context within which the ELC review was being taken forward. Scottish Government guidance explicitly recognises that the rate paid needs to be "sustainable and affordable by the Local Authority", and in the current financial climate any increase beyond the current rate paid would put an unaffordable recurring pressure on Council budgets.

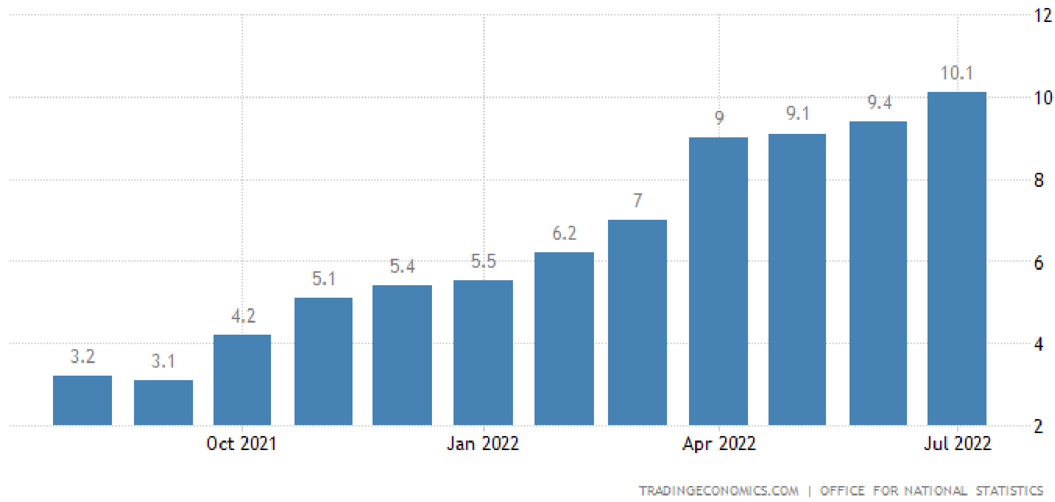
10.7 In light of the financial crisis, the current hourly rate of £5.43 will continue to apply for August 2022 onwards (along with the existing supplement of £0.70 for 2 year old provision and £2.30 per meal provided). At that time the uplifted Highland rate compared to a Scottish average of £5.44. Further discussions will continue as the financial context unfolds and as with all partners expectations regarding reducing costs, reducing energy usage and measures to support staff sustainability will be a focus of engagement.

11. Cost of Living Crisis

11.1 **Inflation, including costs of goods and services**

There are a number of factors influencing the cost-of-living crisis. One such factor is inflation; inflationary increases are detailed in the graph below. The annual inflation rate in the UK increased to **10.1 percent** in July of 2022 from 9.4 percent in the previous period and slightly above market forecasts of 9.8 percent. It was the **highest reading since February 1982**, as prices rose faster across a range of factors, including housing, utilities, food and non-alcoholic beverages, and restaurant and hotels. On the other hand, UK transportation prices eased at a time when consumer prices were above forecasts. Source: Office for National Statistics

11.2

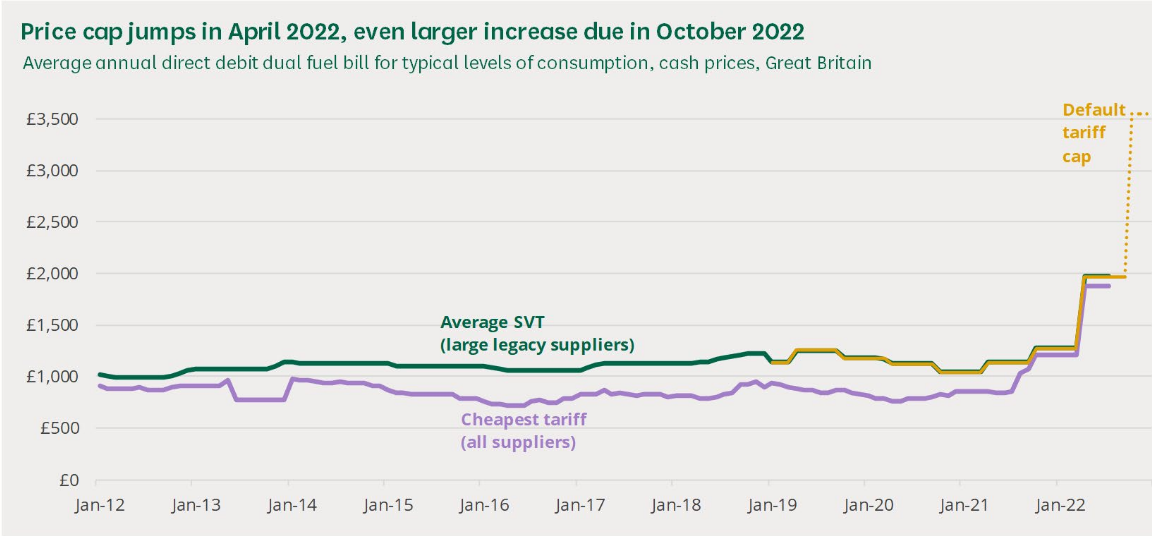


12. Energy Price Increases

12.1 In February 2021, the energy price cap level was increased by 9% to £1,138, which came into effect from April 2021 and in August 2021, the cap level was increased to £1,277 with effect from October 2021. The current energy price cap is £1,971 at typical use and was due to increase to £3,549 this October with an anticipated increase to £5,400 from January 2023. The monthly increases in both gas and electricity prices in April 2022 were by far the largest since 1988 and the annual increases to April 2022 were also the largest ever recorded since 1970.

12.2 The energy price cap increased by 12% in October 2021, 54% in April 2022 and was due to increase by 80% in October 2022 (gas by 91%, electricity by 70%). The April 2022 increase was equivalent to £700 more across a year for ‘typical’ levels of dual fuel consumption households that paid by direct debit and the October cap would have resulted in an increase of almost £1,600. The rapid increase in prices have led suppliers to withdraw cheaper fixed price tariffs and as a result most households are now on Standard Variable Tariffs (SVTs) which are controlled by the price cap. (Source: House of Commons Library)

12.3



13. Cost of Living - Highland Context

13.1 Fuel poverty exists when, after housing costs have been deducted, a household is spending more than 10% (20% for extreme fuel poverty) of their net income to pay for reasonable fuel needs.

13.2 In the latest published figures from the Scottish Household Survey Report 2019, 33% of Highland households were in fuel poverty compared with a Scottish average of 24%, and 22% of Highland households were in extreme fuel poverty compared with a Scottish average of 12%. Note that this survey predates the current energy price crisis so the current scale in Highland shall be much greater.

13.3 At the time of the above research 2017/2018, 63% of Highland households were not on the gas grid (17% for Scotland). These households have not therefore been protected by the energy price cap. The majority of our Highland residents have therefore been subject to the higher costs of other fuel sources, such as oil, Liquefied Petroleum Gas (LPG) and coal.

13.4 Using the same methodology on which the living wage is based, studies have shown that the budgets households need to achieve a minimum acceptable living standard in remote rural Scotland are typically 10-33% higher than elsewhere in the UK. These premiums are most modest for pensioners and greatest for single people and families supporting children. The three principal sources of this increase are: (a) the higher prices that households must pay for food, clothes and household goods; (b) much higher household fuel bills, influenced by climate and fuel sources; (c) the longer distances that people have to routinely travel, particularly to work. It should be noted that when last undertaken in 2016, the overall additional costs were assessed to be slightly lower as a specific result of lower fuel prices at that time. (Source: HIE *A Minimum Income Standard for Remote Rural Scotland, 2016)*

14. Existing supports by the Highland Council

14.1 ***Political Engagement***
The Council is actively engaging with COSLA on the impacts of the cost-of-living crisis and considering options available to local authorities to assist in the current circumstances.

14.2 ***Income Maximisation, Debt, Housing and Energy Advice***
In addition to the welfare services provided by the Council's Welfare Support team, the Council funds Citizens Advice to provide income maximisation, debt and housing advice. The Council also supports Citizens Advice to provide energy advice for households. There is regular promotion via social media of the help that is available and the Worrying About Money? leaflet provides a wide range of relevant financial advice and support together with contact details, and is available in six languages. A cost-of-living webpage has been launched and can be accessed via the home page of the Council's website.

14.3 ***Welfare Budget***
The Council's 2022/23 Welfare Budget exceeds £54m to support low income and vulnerable households. In addition to Housing Benefit and Council Tax Reduction this includes school clothing grants, means-tested free school meals, crisis grants, community care grants to enable continued and settled living in the community, and discretionary housing payments which are intended to reduce shortfalls between the rent liability and financial support available from Housing Benefit and the Housing Element of Universal Credit.

14.3.1 In addition to the above support, a budget of £3.429m was agreed at the Council meeting on 30 June 2022 to provide cost of living support for our vulnerable and low income households.

14.4 ***Out of hours social work and social care services***
Our out of hours social work and social care services provide care at home, emergency supplies and fuel top-ups for those with an identified need.

14.5 ***Employability***
No-one Left Behind provides targeted and responsive services that meet the employability needs of clients and businesses.

14.6 ***Housing Revenue Account – Housing for Council Tenants***
Housing and Property Committee on 31 August 2022 considered several matters relating to the cost-of-living crisis.

14.6.1 A step change in capital expenditure will be required to move towards the Council's Net Zero Carbon target. Loan charges associated with the level of future investment required will place additional pressure on Council House rents.

14.6.2 Rising domestic energy costs are one of the main factors in the cost-of-living crisis. Housing and Property Committee Members discussed the potential to fast track works to properties without insulation in response to rising energy costs and before the onset of winter.

14.6.3 The HRA Capital Programme has prioritised expenditure on energy efficiency measures over many years, with around 60% of the annual programme targeted at these measures. We have invested £23m on new heating, insulation and other energy efficiency measures in the last 5 years. The current 2022/23 HRA Capital Programme has a budget of £9.3m for energy efficiency works. All Council housing has cavity and loft insulation where that is feasible. Future measures are likely to involve an acceleration of internal wall insulation. This is a costly and disruptive measure where there is a limited supply chain and contractor capacity. It is not possible to accelerate the insulation measures at the scale required during the remainder of the financial year due to contractor and material capacity.

14.6.4 Many Council tenants in Highland are amongst our lowest income households yet face the highest energy costs due to utility company policies restricting social rented tenants to prepayment meters.

14.6.5 It is important that we develop a new HRA Capital Plan and Net Zero Carbon strategy for housing that achieves effective targeting of resources and use of new technologies for heating. Preliminary work has taken place to model some of the potential measures involved.

14.6.6 In the meantime, the Housing and Property Committee also approved the use of HRA balances of up to £160,000 this year to fund additional support to assist tenants directly with special independent energy advice and to access financial support.

15. UK Government Energy Price Guarantee (EPG)

15.1 The UK Government's Energy Price Guarantee replaces the Energy Price Cap and is intended to ensure that a typical household will save at least £1,000 a year based on current prices from October. Energy suppliers will be fully compensated for the cost of the Energy Price Guarantee and £150 of the £1,000 saving will be delivered by temporarily suspending green levies. Further information about the EPG was published on the UK Government's website on 8 September 2022 and is available at the following link https://www.gov.uk/government/publications/energy-bills-support/energy-bills-support-factsheet-8-september-2022#support-for-households.

15.2 ***Not connected to the gas grid***
At least 63% of Highland households are not connected to the grid. The UK Government has confirmed that a discretionary scheme will ensure they will be no worse off than those connected to the grid and will receive comparable support.

15.3 ***Fixed Tariff***
Energy suppliers will automatically adjust fixed tariffs to ensure that these customers receive the same level of protection through the EPG as those customers on a standard variable tariff.

15.4 ***Pre-payment meter***
The EPG will be applied to pre-payment meter unit rates, which will continue to be higher than other bill payers as set out in more detail in this report.

15.5 ***Rent includes electricity***
Landlords who include the costs of electricity as part of the rent charge are encouraged to come to an agreement with their tenants about the Energy Price Guarantee. The UK Government is exploring a range of options, including emergency legislation to ensure that such agreements are made.

16. Scottish Government Programme for Government 2022 to 2023

16.1 The Scottish Government's Programme for Government is published each September and for 2022 to 2023, it focuses on the immediate priorities which the Government considers should be progressed. Published on 6 September 2022, The Programme for Government is available at the following link https://www.gov.scot/publications/stronger-more-resilient-scotland-programme-government-2022-23/pages/2/ and contains the following commitments.

16.2 ***Scottish Child Payment***
From 14 November 2022, the Scottish Child Payment will increase from £20 to £25 per week per eligible child and be extended to include children and young people aged between 6 and 15.

16.3 ***Universal Provision of Free School Meals for P6s and P7s***
Subject to agreement with COSLA, begin to roll out the provision of universal free school meals to Primary 6 and Primary 7 pupils, and take further action to reduce the cost of the school day for families, including reducing the cost of school uniforms through new guidance.

16.4 ***Fuel Insecurity Fund***
Through the Emergency Budget Review, increase the Fuel Insecurity Fund from £10m to £20 million in 2022-23, to help households at risk of self disconnection or self-rationing of energy use as the energy price cap rises from October.

16.5 ***Tenant Grant Fund***
Widen eligibility for the Tenant Grant Fund to support those struggling with increasing costs.

16.6 ***Winter Heating Payments***
Introduce Winter Heating Payments which guarantee a £50 annual payment for low-income households.

16.7 ***No-interest loan scheme***
Invest in a no-interest loan scheme pilot to help people in Scotland access affordable credit. The scheme will enable people on lower incomes who cannot afford to repay interest, including from community lenders, to access short-term credit to meet unexpected costs.

16.8 ***Cash-first approach and end the need for foodbanks***
Prioritise urgent action this winter to strengthen cash-first support and publish a plan to end the need for food banks.

16.9 ***Discretionary Housing Payments***
Increase Discretionary Housing Payment funding to mitigate the benefit cap and provide local authorities with more flexibility to take account of energy bills when deciding Discretionary Housing Payments.

17. Cost of Living – Highland Council Overarching Guiding Principles

17.1 The Council does not have the legal or fiscal powers to decide the necessary legislative and structural changes, and financial packages of support, to mitigate or suppress the cost-of-living crisis for Highland residents. The welfare proposals set out in this report are therefore intended to help alleviate rather than mitigate the significant pressures which are impacting households across the Highlands.

17.2 A key focus of the welfare proposals set out in this report is to enable residents to eat, to heat their living areas, and to continue to live safely in their homes. The support proposals set out in this report have been designed to achieve ease of access, a cash-first approach, and automatic awards where applicable, while enabling support to be provided for our most vulnerable residents.

17.3 The Council will continue to promote the wide range of community-led supports already operating across Highland. These include food and activities for young people/families during the school holiday periods, local food larders and food fridges, provision of food, and community growing projects.

17.4 **Appendix 3** to this report is provided for illustrative purposes and details scenario energy bills to reflect some typical household compositions. These calculations do not include non-energy specific supports, such as Housing Benefit and Council Tax Reduction and are based on the energy-related supports available from the UK and Scottish Governments. For example, based on the UK Government's Energy Price Guarantee of £2,500, a 79 year old pensioner in receipt of Attendance Allowance will receive a range of supports, which will reduce their energy bill to £1,190. A family of four with a child with an additional support need, earning £29,000 per annum, which can access the £140 Warm Home Discount scheme, will be able to reduce their bill by £1,554.10 in energy-related support.

18. Cost of Living Crisis Proposals

18.1 It is proposed that the Council allocates £3.223m non-recurring funding from its non-earmarked reserves for the provision of both direct support and community-led initiatives.

18.2 The proposals are summarised below.

Support	**Allocation from non-earmarked reserves**
Cost of Living Support - £145 per eligible household	£2.523m
Free School Meal Weekend Holiday Payments	£0.200m
Community-led initiatives	£0.450m
FareShare	£0.050m
Total from non-earmarked reserves	**£3.223m**

18.3 ***Cost of Living Support- £2.523m***
Using the Council's non-earmarked reserves, it is proposed to make non-recurring payments of £145 each to around 17,400 council tax payers who are receiving some form of reduction from their council tax bills through means-tested Council Tax Reduction or exemptions from Council Tax based on personal circumstances. These personal circumstances are set out in Council Tax legislation as (a) individuals with a Severe Mental Impairment, (b) those who are not residing in their main home as they are providing or receiving care elsewhere, and (c) those who are aged under 18 who are liable for Council Tax. Cost of Living Support payments will be paid to those eligible for these reductions as at 31 August 2022 with a council tax liability. Where the relevant information is held by the Council, it is proposed to automatically make a one-off payment of £145 to each eligible council taxpayer by 30 November 2022.

18.4 ***Free School Meal Weekend Holiday Payments - £0.200m***
Low income families already receive free school meal payments for Mondays to Fridays (inclusive) during each of the school holiday periods. It is proposed to extend these payments to cover weekends during the remaining school holidays up to including Easter 2023.

18.5 ***Community Led Initiatives - £0.450m***

Building on the learning from the pandemic, it is proposed to create a Highland-wide grant fund to support communities to respond to the cost of living crisis. Community led support enables a local response to address local needs which will complement any individual support payments.

18.5.1 Grants of up to £10k per organisation would be made available with the aim of this grant fund to enable community groups to provide local activities and support. The proposed criteria for the fund are as follows:

- Provide community support initiatives that provide food/activities
- Enhance existing provision through extending local hours or introducing/increasing food provision
- Adapt existing provision to meet identified local needs
- Strengthen or establish food larders or food table provision

18.5.2 To enable grants to be issued at pace, grant fund decisions are delegated to the ECO – Communities & Place, supported by Ward Managers and the Community Support and Engagement team. Awards will be reported to the Communities & Place Committee, which will keep this fund under review. Grants can be applied for by constituted community groups through the well-established single grants process.

18.5.3 The availability of the fund will be promoted through the existing community resilience network and Community Support Co-ordinators will work with local groups to support the development of proposals in order to respond to local need.

18.6 **FareShare Highland - £0.050m**

Locally based, FareShare is the main distributor of surplus food to community groups across the Highlands. During August 2022, FareShare distributed 13.38 tonnes of surplus food; the equivalent of 31,860 meals for 3,840 beneficiaries, with a retail value of around £18,000. FareShare continues to expand its membership base and during August 2022, welcomed community groups in the Black Isle, Caithness and Evanton, renewed its relationship with the Skye Food Bank and has increased the supply of food in Caithness. It is therefore proposed to provide non-recurring funding of £0.050m to FareShare for the purchase of food for distribution across the Highlands.

19. Future Look

19.1 The Council will continue to monitor the supports available from the UK and Scottish Government, fluctuations in the inflation rate and wider impacts that impact upon the cost of living for our residents and will provide further reports to Council as required.

Designation: Chief Executive

Date: 14 September 2022

Authors: Sheila McKandie, Interim Head of Revenues & Business Support
Edward Foster, Head of Finance
Elaine Barrie, Interim Head of People
Nicky Grant, Executive Chief Officer, Education
Brian Porter, Head of Resources, Education

David Goldie, Head of Housing and Building Maintenance

Background Papers: UK Government Energy Price Guarantee
Scottish Government Programme for Government
https://www.highland.gov.uk/download/meetings/id/80418/5a_corporate_revenue_monitoring_to_30_june_2022

Appendix 1

Cabinet Secretary for Finance and Economy
Kate Forbes MSP

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Councillor Alison Evison
COSLA President
Verity House
Edinburgh
EH12 5BH

Copy to: The Leaders of all Scottish local authorities

31 May 2022

Dear Alison,

Earlier today, as part of a statement to Parliament, I published the Scottish Government's Resource Spending Review. The Review is ambitious but realistic. In setting high level multi-year portfolio spending envelopes it offers a strategic funding framework for the Scottish Government and our many partners to plan for the future. That of course includes local government which has such a significant role to play in so many areas of government.

Fiscal Context

Whilst the UK Government has belatedly taken action to mitigate some of the impact of rising energy prices on households, it has not responded to address the broader impact of inflation on business and public services.

The UK Spending Review in October 2021 set out a funding cash envelope for the Scottish Budget at a time when inflation was significantly lower and as a consequence the true spending power of those funding envelopes has already been significantly eroded. To date the UK Government has chosen not to adjust spending plans to reflect this and funding available for investment in public services through the rest of this parliament remains constrained. I would welcome the opportunity to discuss with you on what we might do collectively to raise this with the UK Government and the public in Scotland.

As you will be aware, the Scottish Budget for 2022-23 was already reduced in real terms by 5.2% relative to 2021-22 and growth in spending capacity over the rest of the parliament, once social security transfers are excluded, remains at only 2%. This low level of investment is deeply damaging to public services and once again highlights that Scotland does not currently hold the levers required to address our most pressing challenges.

The central funding position outlined in the spending review reflects a range of assumptions to inform the official forecasts, and are based on current tax policies as forecast by the Scottish Fiscal Commission. The funding envelopes set out here are indicative currently of what we can reasonably expect over the spending review years, including assumptions about additional consequential funding from UK Government beyond the spending review settlement and revenues accruing from Scotwind, but it is our annual budgets which will confirm these.

Similarly, the funding envelopes are presented at portfolio level (Level 2) and are therefore not as granular as the allocations published alongside the budget. This approach is critical so as not to constrain portfolios in the choices they make in support of our strategic priorities but does have implications for the level of detail available to make comparisons with previous years. These details, including any in-year transfers, will be confirmed as part of the annual budget process.

Vision

Despite the challenging fiscal context, the resource spending set out in this review will drive the Scottish Government's ambitious vision for Scotland's public services. We are committed to strong, responsive public services which serve individuals' needs, improve national outcomes and create the right opportunities for Scotland to be healthier, happier and more prosperous. We want public funding to build a Scotland where communities are inclusive and empowered, and people grow up loved and respected, well-educated, and healthy. I know you and other council leaders share much of this vision.

In order to achieve this, this spending review provides fresh impetus to our public services reform programme and sets out a coherent package of action that will drive progress over the life of the current Parliament, improving outcomes while driving efficiency and value for public money.

While key elements of this vision will not directly apply to local government, addressing the financial challenges facing Scotland's public services would benefit from a cross-public sector approach in order to optimise the reach of public funding to deliver the best possible services and support to our people and communities. I would therefore anticipate and welcome a complementary approach across all parts of the public sector landscape.

This package includes:

- Changes to working practices, with our Fair Work principles at their heart, to support greater flexibility and continued hybrid working across the public sector;
- A pathway to return the overall size of the public sector workforce broadly to pre-

COVID-19 pandemic levels, while supporting expansion in key areas of service delivery, helping to hold total pay bill costs - as opposed to pay levels - at 2022-23 levels;

- Support through public sector pay arrangements for those on the lowest incomes faced with the hardest impacts of the cost of living crisis;
- An enhanced focus on delivering efficiency savings across the public sector, while recognising existing efficiency programmes in some sectors, which we will support through a variety of levers including;
- Fresh consideration of the public body landscape, with further engagement ahead of the next Budget about a programme of reform;
- A multi-year estates programme to make the best use of public sector property and other assets, reflecting the impact of the COVID-19 pandemic on ways of working and the delivery of services;
- An increased focus on maximising revenue through innovation, reflecting the guidance in the Scottish Public Finance Manual;
- A programme of digital reform, focused on inclusion and connectivity, developing a strong digital economy and investment in digital transformation of public services;
- The development of a strategy for public procurement that will drive greater collaboration and value for money.

I look forward to working with the new COSLA Leadership to explore how local authorities might contribute to that approach alongside the development of a new deal for local government. I will also ensure the relevant Scottish Government officials are available to COSLA to discuss the details set out in this package. I know that some local authorities have already undertaken similar reforms already and there will be the opportunity also to learn from their experience, which I would welcome.

Local Government Settlement

Reflecting the fact that Local Authorities are key partners in the delivery of the priorities set out by the spending review, the spending review baselines the £120 million added during the 2022-23 Budget Bill process and maintains General Revenue Grant, Non-Domestic Rates Income and Specific Resource Grants between 2023-24 and 2025-26 before adding a further £100 million in 2026-27.

As the majority of in-year transfers from other portfolios apply to Level 4 budgets, the strategic approach of publishing portfolio allocations at Level 2 in the spending review precludes a direct like with like comparison with previous years' overall settlement figures. Final details of the settlement including additional transitional funding to reflect the devolution of Empty Property Relief to Councils from 1 April 2023; confirmation of the approach adopted for in-year transfers; and individual Council allocations will be confirmed alongside the annual budget process.

The spending review affirms the Scottish Government's commitment to agreeing a 'new deal' for Local Government in Scotland through the development of a Partnership Agreement and Fiscal Framework. The new deal will build on the Review of Local Democracy and seek to balance greater flexibility over financial arrangements for local government with increased accountability or the delivery of national priorities so that both partners can have certainty over inputs and outcomes alongside scope to innovate and improve the delivery of services to local people and communities.

This joint aspiration coupled with the strategic approach to portfolio allocations means that the spending review makes no assumptions about the scale and scope of any transfers to local government from other portfolios in-year. However, to offer a degree of certainty, the spending review confirms that existing in-year transfers for Health and Social Care, Early Learning and Childcare and additional Teachers worth £1 billion combined will be maintained. Final decisions on the transfers from other portfolios in future years will be confirmed following the establishment of the Fiscal Framework.

The spending review also makes no assumptions about council tax nor about greater scope for discretionary revenue-raising, such as the Visitor Levy and the newly created Workplace Parking Levy, as decisions about further fiscal autonomy will be part of ongoing discussions to establish and agree the Fiscal Framework.

Alongside the resource spending review, we have also conducted a targeted review of our capital spending plans, to deal with much lower-than-expected funding from the UK Government, and to ensure capital investments align with government priorities, as set out in the Programme for Government and Bute House agreement. Whilst final allocations will be confirmed as part of the annual budget process, there are no changes to the Local Government capital allocations as set out in my letter to the COSLA President dated 4 February 2021.

Fiscal Flexibilities

In my letter to you on 9 December 2021 alongside the budget, I confirmed my intention to allow an extension of the flexibilities to allow capital receipts to be used to fund the financial impact of COVID and to fund transformational projects subject to confirmation from the UK Government that this will not result in an adjustment to Scotland's block grant.

Unfortunately, the UK Government recently rejected my request and confirmed that any use of this flexibility to fund the financial impact of COVID will result in an adjustment to Scotland's block grant. Given the constrained fiscal position, I am therefore no longer able to offer that specific flexibility to deal with the impact of COVID although the offer of flexibility on using receipts for transformational projects remains unchanged.

In that letter, I also outlined my commitment to continue working with Directors of Finance and CIPFA/LASAAC on a Capital Accounting Review. I have now received a copy of the conclusions of the Directors of Finance's review. I am extremely grateful to Directors of Finance for their work on that review but having considered their findings, it falls short of the comprehensive review that was anticipated at the outset of these discussions. As noted by both Audit Scotland and LASAAC, the review focuses on capital funding arrangements and on maintain existing statutory mitigation but does not deliver proposals for closer alignment with accounting standards.

The spending review therefore confirms the Scottish Government's intention to commission an independent Capital Accounting Review. The independent review will build on the review already taken forward by Directors of Finance working with key stakeholders to deliver a phased approach towards alignment with the CIPFA Code of Practice for Local Authority Accounting.

This review will help to enhance the future sustainability of local services and address the inconsistencies of current statutory arrangements with the requirements of the CIPFA Accounting Code but I acknowledge that it will not address the long-standing request from COSLA on flexibility regarding the accounting treatment of service concessions.

On 1 February 2022, I wrote to CIPFA/LASAAC inviting them to offer an independent view on COSLA's request, which had of course been substantially changed when Directors of Finance acknowledged that a key part of the original request would have been inconsistent with recognised accounting practice. I have now received their response to the amended request and whilst I am very grateful to CIPFA LASAAC for their consideration, the response was ultimately inconclusive on the key aspects. The fact that CIPFA/LASAAC were unable to provide a conclusive resolution to this does highlight the risks of statutory intervention and the need for a comprehensive review.

In light of the withdrawal of the request to capitalise interest payments, I am willing to accede to the request to recognise principal debt repayments over the asset life and for this approach to be applied retrospectively. I will also agree that this may apply to the grant funded element of the principal debt repayments. .

This flexibility will only apply to existing service concessions and each local authority will be responsible for fully evaluating any change in method and making appropriate financial provision. The decision for making any change must be taken by the Council, that is, it may not be delegated. The Minister for Public Finance, Planning and Community Wealth will provide further details on the statutory mitigation and the remit of the independent review in due course. We will of course welcome your input to the scope and design of that review.

Conclusion

The spending review does not alter the parliamentary requirement for an annual budget process but it does provide the multi-year certainty requested by COSLA on numerous occasions. It guarantees the combination of General Revenue Grant and Non-Domestic Rates income at current levels despite a challenging UK Government Settlement and offers protection against Non-Domestic Rates revenue uncertainty post-COVID-19 and ahead of the 2023 revaluation with the addition of a further £100 million in 2026-27.

Due to the strategic nature of the portfolio allocations, it is not possible to prepare direct comparison with previous years but the spending review provides funding certainty over key transfers for Teachers and Health and Social Care. The spending review also reaffirms our commitment to working with COSLA and SOLACE to agree a new deal for Local Government in Scotland in advance of the next financial year and I look forward to commencing those discussions with the new COSLA Leadership in due course.

Yours sincerely.

KATE FORBES

Appendix 2

An Leas-phrìomh Mhinistear agus Ath-shlànachadh Cobhid
Deputy First Minister and Cabinet Secretary for Covid Recovery
John Swinney MSP

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Councillor Katie Hagmann
COSLA Resources Spokesperson

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sally@cosla.gov.uk
Local Authority Leaders

18 August 2022

Dear Councillor Hagmann,

Thank you for the meeting on 17 August with yourself, Councillor Morrison and Councillor Heddle to discuss the current pay position.

At the meeting I set out the current challenging Scottish Government budget position, with the 2022-23 Scottish Budget fully committed against a backdrop of inflationary pressures and the cost crisis. Indeed, the Scottish Fiscal Commission has highlighted the overall 2022-23 Scottish Budget is 2.6% lower than last year in cash terms primarily because of reduced Covid-19 funding and falling capital funding from the UK Government.

We are all experiencing unprecedented pressures on public finances, which have been further exacerbated with the increase in inflation and the situation in Ukraine. Nevertheless, the Scottish Government has made difficult decisions across our public service provision to offer the financial contribution of £140 million in recurring funding to local authorities in order to support a revised pay offer.

All areas of the public sector will have to make challenging savings to live within existing budgets. The UK Government has not provided further funding for these pressures, with last year's UK Spending Review not taking account of the levels of pay uplift now proposed or the wider effects of inflation.

Turning to fiscal powers, the Scottish Government has limited borrowing powers, and is not permitted under the relevant statutory arrangements to revisit sufficiently significant revenue raising policies, such as income tax, in-year.

A number of comments have been made stating the Scottish Government should utilise the funding in its reserves. I do not recognise the numbers being discussed, as the Scottish Government has used reserves in full to deliver the 2022-23 budget. Indeed, the additional £120 million provided to local government at stage 2 of the 2022-23 budget was delivered through the use of the Scotland reserve. Given that, and now the offer of a further £140 million to support a pay deal, any suggestion that we have not fully utilised all avenues open to us to provide additional funding to councils is wholly unfounded. I would again encourage all councils to consider the use of reserves for other short term cost pressures so as to redirect resources to the pay offer.

Throughout our discussions I have sought to work collaboratively while providing full transparency around our financial position, as part of this I have set out the reserve position in detail in Annex A. I would also note, much like borrowing, the Scottish Government has very limited reserve powers (with the ability to only hold £700 million in reserve, which is under 2% of the full Scottish Government budget), with Local Government having greater powers in this respect.

As I have previously made clear, the Scottish Government is not in a position to provide a further additional contribution and I would ask councils to again consider carefully how they too could increase available funding for pay. I would also note that it is councils which are the employers here and there is no direct role for the Scottish Government in this relationship.

It is essential that urgent action is now taken; I do not need to tell you that waste collection services in Edinburgh will strike from today and that further action in the weeks following has already been called across a number of councils. Moreover, council employees now face the prospect of meeting inflationary pressures on their cost of living this autumn without having received a pay increase from their employers.

I know difficult decisions will need to be made by Local Government to meet the pay offer. This is equally the case for the Scottish Government, and I would emphasise that if we are to have a mature partnership that we must both recognise this shared reality.

Finally, at our meeting I committed to looking at any detailed proposals that COSLA will put forward for flexibilities with regards policy delivery and the use of reserves. While this work is underway, it is critical that a meaningful, revised offer is made at pace, and that negotiations with the Unions proceed to reach a swift agreement.

I look forward to hearing from you,

JOHN
SWINNEY

Annex A Scottish Government

Reserves Position Scotland Reserve Background

The Scotland Reserve provides the Scottish Government with a limited facility to manage the smoothing of all types of spending, assist the management of tax volatility and determine the timing of expenditure.

The Reserve is split between Fiscal Resource and Fiscal Capital and is capped in aggregate at £700 million.

In normal times, annual drawdowns from the Reserve are limited to £250 million for Fiscal Resource and £100 million for Fiscal Capital (including Financial Transactions) in any given year.

However, in the event of a 'Scotland-specific economic shock', this cap on draw down does not apply.

Scotland Reserve 2022-23 Position

At the 31st March 2022 funding of £650 million was transferred to the Scotland Reserve,

£421 million of this was Resource funding. **All** of the £650 million is being utilised to support 2022-23 (i.e. there is no remaining funding in reserves), and is reflected in the latest 2022-23 Resource, Capital and FT position.

	Resource	Capital	FTs	Total
	£m	£m	£m	£m
Provisional Outturn Underspend (2021-22)	(421)	(183)	(256)	(860)
Repayment of Financial Transactions to HM Treasury			210	210
Provisional Scotland Reserve Position (2021-22)	**(421)**	**(183)**	**(46)**	**(650)**
2022-23 Budget Bill targeted carry forward balance	332	118	61	511
Reserve draw down planned for 2022-23 ABR	89	65	(15)	139
Balance available	**-**	**-**	**-**	**-**

Much of the carried forward funding was anticipated within the 2022-23 Scottish Budget;

£324 million was anticipated within the initial 2022-23 Budget, and £120 million was announced by the Cabinet Secretary of Finance and Economy to support Local Government 2022-23 costs at stage 1 of the Budget Bill process. Overall the targeted Scotland Reserve carry forward in the 2022-23 Budget Bill was £511 million. The remaining £139 million of the

£650 million in the Scotland Reserve will be disclosed to Parliament as part of the Autumn Budget Revision (ABR) process but as noted above is already factored in to the latest 2022- 23 position.

Appendix 3

Scenario Energy Bills – For illustrative purposes only
(Produced by The Highland Council – Head of Revenues & Business Support)

Household composition					
These scenarios include working age adults not in receipt of benefits, working age adults in receipt of benefits, households with disabled adults and those with disabled children, and pensioners. LACER support agreed at 30 June 2022 Council is not included in this table.	**Highland Household 1** Working age adults Both working full time No children	**Highland Household 2** Single pensioner, aged 79 years In receipt of Attendance Allowance	**Highland Household 3** Pensioner couple both aged 81 years	**Highland Household 4** 2 working age adults 2 children Working part-time, In receipt of Universal Credit, Child Disability Payment for 1 child (high-rate care)	**Highland Household 5** 1 adult under 25 years, 1 child In receipt of Universal Credit.
*Household income before housing costs are deducted	£57,000	£16,000	£35,000	£29,000	£5,650
Energy Price Guarantee	**£2,500**	**£2,500**	**£2,500**	**£2,500**	**£2,500**
Energy Bill Support Scheme	- £400	-£400	-£400	-£400	-£400
One-off Cost of Living Payment for those on means tested benefits	0	0	0	-£650	-£650
Disability Cost of Living Payment	0	-£150	0	-£150	0
Winter Fuel Payment including one-off Pensioner Cost of Living Payment	0	-£500	-£300	0	0
Warm Home Discount scheme**	0	-£140	0	-£140	-£140
Child Winter Heating Assistance	0	0	0	-£214.10	0
Total energy-related/cost of living support	**£400**	**£1,190**	**£700**	**£1,554.10**	**£1,190**

Potential Household energy cost	£2,100	£1,310	£1,800	£945.90	£1,310

*For illustration and is for information purposes only, household outcomes will depend on individual circumstances

****The Warm Home Discount scheme is decided and operated by individual suppliers and the number of discounts suppliers can award to their customers is limited. Accordingly, even if a household meets their supplier's eligibility criteria, they may not receive the £140 discount.**

Energy Price Guarantee: From 1st October, the new 'Energy Price Guarantee' is intended to mean a typical UK household will pay no more than £2,500 a year on their energy bill for the next two years. This is automatic and applies to all households. This will save the average household at least £1,000 a year based on current energy prices from October and is in addition to the £400 energy bills discount for all households. This applies to all households in Great Britain.

Energy Bills Support Scheme: Households will receive **£400** of support as credits to their energy bills. Energy suppliers will deliver this support automatically to households with a domestic electricity meter over six months from October. Direct debit and credit customers will have the money credited to their account, while customers with pre-payment meters will have the money applied to their meter or paid via a voucher.

One-off Pensioner Cost of Living Payment: Pensioner households will receive an extra £150 - £300 to help them cover the rising cost of energy this winter. This additional one-off payment will be made to households who receive the Winter Fuel Payment and will be paid on top of any other one-off support a pensioner household is entitled to. These amounts are for winter 2022 to 2023.

Disability Cost of Living Payment: A one-off payment of £150 will be made to people who receive one of the following: Constant Attendance Allowance, Disability Living Allowance for adults, Disability Living Allowance for children, Personal Independence Payment, Adult Disability Payment (in Scotland). Child Disability Payment (in Scotland), Armed Forces Independence Payment, War Pension Mobility Supplement. This one-off payment will made in addition to any other support payment the household is entitled to receive.

Recipients must have received a payment (or later receive a payment) of one of these qualifying benefits for 25 May 2022 to get the payment. You'll be paid the £150 Disability Cost of Living Payment automatically from 20 September 2022. Most people will receive their payment by the beginning of October 2022.

Winter Fuel Payment: A Winter Fuel payment is a one-off, tax-free payment of between £100 and £300 made during the winter to help with heating costs; it is made to households with someone over Pension Credit age. Most payments are made automatically during November and December. If someone applies for the first time, they will receive their payment by Christmas. The amount a household will receive each winter can vary according to their personal circumstances. For example, age or other people living in the house who are also eligible can increase the eligible amount.

The Warm Home Discount scheme: The Warm Home Discount scheme (WHDS) is a limited fund which offers a one-off payment of £140 (inclusive of VAT) towards energy bills of those who need it most. The scheme was introduced by the UK Government in April 2011 and is managed by energy suppliers. The money isn't paid directly to the customer; it is a one-off discount that is credited to the customer's energy account, prepayment card or key, during the winter.

There are 2 ways to qualify for the Warm Home Discount Scheme:

- if someone gets Pension Credit Guarantee Credit; **or**
- someone on a low income who meets their energy supplier's criteria for the scheme.

How someone applies for the Warm Home Discount Scheme depends on how they qualify for the discount and not everyone who is eligible for a discount will receive one due to the limited nature of the fund.

Child Winter Heating Assistance: is a payment for children and young people up to the age of 18. To get the payment they must meet two criteria on at least one day in the third full week of September (called the "qualifying week"). On that day they must if they're under 19 years old and get one of the following 'qualifying benefits':

- the highest rate of the care component of Child Disability Payment
- the highest rate of the care component of Disability Living Allowance for children
- the enhanced daily living component of Personal Independence Payment
- the enhanced rate of the daily living component of Adult Disability Payment
- be resident in Scotland

If there is more than one child or young person in a qualifying household, they will all receive the payment. In 2022, the payment will be £214.10 per eligible child.