

**ITEM No ...4.....**

**REPORT TO: POLICY AND RESOURCES COMMITTEE – 25 JANUARY 2021**

**REPORT ON: FINANCIAL OUTLOOK AND REVENUE BUDGET 2021/22**

**REPORT BY: CHIEF EXECUTIVE**

**REPORT NO: 51-2021**

**1.0 PURPOSE OF REPORT**

This report advises members of the financial outlook at a national level following the recent UK Spending Review announcements. The report also outlines the current position on the Council's Revenue Budget for 2021/22, in terms of required savings.

**2.0 RECOMMENDATIONS**

It is recommended that the Committee:

- 2.1 Notes the financial outlook at a national level.
- 2.2 Notes the range of projected savings that may be required for 2021/22 in order to deliver a balanced budget.
- 2.3 Approves the update to the Long-Term Financial Strategy, as set out in paragraph 9.2 of this report.
- 2.4 Notes that a further report will be submitted to the Policy and Resources Committee on 22 February 2021, detailing the Council's actual grant settlement for 2021/22 and the associated implications. This report will include the proposed procedure for setting the Council's Revenue Budget and Council Tax for 2021/22.
- 2.5 Notes that it is anticipated that the Policy and Resources Committee will meet on 4 March 2021 to set the Council's 2021/22 Revenue Budget and Council Tax.

**3.0 FINANCIAL IMPLICATIONS**

- 3.1 Based on different scenarios for the grant settlement and the pay award, the range of savings required in order to set a balanced budget for 2021/22 is as follows:

	Grant Settlement 2021/22 (% Change from 2020/21)			
	0%	-1%	-2%	-3%
Pay Award 2021/22				
1%	£ 5.3 m	£ 8.2 m	£ 11.3 m	£ 14.2 m
2%	£ 7.5 m	£ 10.5 m	£ 13.5 m	£ 16.4 m
3%	£ 9.7 m	£ 12.7 m	£ 15.7 m	£ 18.6 m

- 3.2 In line with the approved Long-Term Financial Strategy, the current financial projections assume that demographic growth will not be funded given the scale of the financial challenge. Rather, all services are expected to redesign services and work in partnership with other bodies to meet the cost of additional pressures.

**4.0 BACKGROUND**

- 4.1 The long-term financial outlook and financial strategy for 2020 to 2030 were set out in Report 274-2019, which was submitted to the Policy and Resources Committee on 19 August 2019 (article XII refers). The report identified that £78.1m of savings and efficiencies may be required over the 10-year period 2020-2030 in order to achieve a balanced budget.

4.2 The Council's Revenue Budget for 2020/21 was agreed by the Policy and Resources Committee on 5 March 2020 (article II refers). In the covering budget report 109-2020, it was projected that additional savings of £9.1m would be required to achieve a balanced budget in 2021/22 (on the assumption that a balanced budget was set for 2020/21). This figure subsequently reduced to £7.5m as a result of decisions taken when setting the 2020/21 budget.

4.3 Elected members will recall that national and local budgeting processes were delayed last year due to uncertainties around Brexit and the calling of a General Election on 12 December 2019. Subsequently, the national response to the Covid-19 epidemic has seen unprecedented levels of unplanned public sector spending, both in terms of measures to contain and fight the spread of the virus and to deal with the economic impact. This has added significantly to the uncertainties around the financial outlook for the UK economy in general and for the public sector specifically. In turn, this creates a great deal of uncertainty around the appropriateness of the Council's existing budget assumptions, particularly grant funding levels.

#### 5.0 SPENDING REVIEW 2021/22

5.1 On 25 November 2020, the Chancellor of the Exchequer published a one-year UK Spending Review covering the 2021/22 financial year. This sets out the 2021/22 spending plans for the various departments of state, including the devolved administrations. The Spending Review announcements were accompanied by updated economic forecasts by the Office for Budget Responsibility (OBR). The forecasts reflect three different scenarios (upside / central / downside), largely based on different outcomes for economic recovery from Covid-19 and assuming an orderly transition Brexit deal. The key economic measures, based on the central scenario, are set out in Table 1 below.

**Table 1: Key UK Economic Measures (Central Scenario)**

	2019	2020	2021	2022	2023	2024	2025
Gross Domestic Product (real terms)	1.3%	-11.3%	5.5%	6.6%	2.3%	1.7%	1.8%
Unemployment	3.8%	4.4%	6.8%	6.5%	5.4%	4.5%	4.4%
Inflation (CPI)	1.8%	0.8%	1.2%	1.6%	1.7%	1.9%	2.0%
Interest Rates	0.8%	0.1%	0%	0%	0.1%	0.2%	0.4%

Key points to note from Table 1 are:

GDP – after a dramatic fall in 2020 there is a two-year recovery period before growth returns to more typical rates, with longer term growth rates remaining relatively poor.

Unemployment – is projected to peak at 7.5% in the second quarter of 2021.

Inflation – currently low and not expected to return to target rate (2%) until 2025.

Interest Rates – expected to remain at low levels

Table 2 below sets out the key measures for the UK public finances.

**Table 2: UK Public Finances – Key Measures**

	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26
Receipts (£bn)	828	771	847	886	927	964	1,004
Expenditure (£bn)	884	1,165	1,012	991	1,027	1,064	1,106
Borrowing (£bn)	56	394	164	105	100	100	102
Debt as % of GDP	86%	105%	108%	109%	109%	105%	105%

Key points to note from Table 2 are:

Receipts – significant reduction in current year due to impact of economic slow-down on income tax, VAT and business tax receipts.

Expenditure – significant increases due to additional unplanned expenditure related to Covid-19.

Borrowing – significant increases as a result of reduced receipts and increased expenditure.

Debt as a % of GDP – is now above 100% and is expected to remain fairly steady at this level.

- 5.2 For Scotland, resource (or day-to-day) spending is set to increase by £1.3bn, from £30.4bn in 2020/21 (the final spending limit prior to the additional Covid-19 related funding in-year) to £31.7bn in 2021/22. This equates to a 4.3% increase, compared to an increase of around 7.4% between 2019/20 and 2020/21 (£28.3bn to £30.4bn). Capital spending is set to fall from £5.5bn in 2020/21 (again, this is the final spending limit prior to the additional Covid-19 related funding in-year) to £5.2bn in 2021/22. Covid-19 related funding is set at £1.3bn for 2021/22, compared with the guaranteed minimum amount of £8.2bn in 2020/21. When the planned resource spending for 2021/22 is combined with the planned Covid-19 related funding, this means that there will be £33bn for Scotland's day-to-day spending next year.
- 5.3 The Chancellor's Spending Review announcements also included reference to public sector pay policy. NHS staff in England will receive pay increases in line with future Review Body recommendations. Other public sector employees will be subject to a "pay pause" although lower paid employees will receive a minimum £250 increase. The National Living Wage for those aged 23 and over will increase by 2.2%, from £8.71 to £8.91, in line with the recommendations of the Low Pay Commission. It is emphasised that the Chancellor's announcements on public sector pay policy relate only to England. Public sector pay policy in Scotland is a reserved matter for the Scottish Government and initial ministerial statements suggest a less constrained policy will be adopted. Further, local government in Scotland has its own dedicated negotiating mechanisms for agreeing pay awards, with separate mechanisms in place for teachers and local government employees. In summary, the Spending Review announcements offer little guidance in terms of the likely level of pay awards that Scottish Councils will have to fund in 2021/22. By way of background, it should be noted that the SJC Trade Union Joint Secretaries have recently lodged a pay claim for 2021 that includes a £2,000 flat rate increase to all spinal column points or 6% (whichever is greater) and an underpinning minimum rate of pay of £10.50 per hour.
- 5.4 The Chancellor's Spending Review announcements will help inform the Scottish Government's budget process, however they offer little insight as to the likely level of government grant support that the Council will receive for 2021/22.
- 5.5 To some extent, the 2020 Spending Review has been a holding exercise, with the key budgetary decisions around taxation, spending commitments and sustainable debt levels still to be taken. It is anticipated that some clarity on these issues will start to emerge in the Chancellor's Spring 2021 Budget.

## 6.0 **FINANCIAL IMPLICATIONS OF THE COUNCIL'S RESPONSE TO THE COVID-19 EMERGENCY**

- 6.1 The Covid-19 emergency has impacted on all areas of society and on all aspects of normal daily life and a further full national lock-down has recently been introduced . These impacts have been severe and are likely to continue for some time, even after the roll-out of the vaccination programme. All levels of government have taken action to support and protect our most vulnerable citizens, local businesses, key suppliers and the third sector during these challenging and unprecedented times. These actions seek to maintain resilience during this crisis and ensure that people and organisations will emerge in the best possible shape when the emergency is over. The financial implications of the public sector response have been significant and have required record levels of unplanned spend.
- 6.2 Report 308-2020 was considered by the Policy and Resources Committee on 7 December 2020. The report set out an update on the financial implications of the Council's response to the Covid-19 emergency and the associated financial recovery plan. Projections in the report show gross additional costs of £37.113m for financial year 2020/21, in respect of the Council's response to the Covid-19 emergency. This includes £5.490m for LACD. At this stage, it is assumed that the additional costs incurred by DHSCP in addressing the Covid-19 emergency will be funded in full by the Scottish Government. After taking into account confirmed additional government funding streams, the projected funding shortfall for 2020/21 is £18.166m. The financial recovery plan contains various measures aimed at mitigating the increased costs in financial year 2020/21 to protect the Council's financial sustainability going

forward. The financial recovery plan currently totals £11.635m, leaving a projected deficit of £6.531m for 2020/21. A further report will be submitted to the Policy and Resources Committee on 22 February 2021 to advise elected members of progress in aligning 2020/21 spend levels more closely with the funding available.

6.3 Report 308-2020 also advises that three financial flexibilities have been made available by the Scottish Government to help Councils to mitigate (or at least defer) the financial impact of Covid-19. These financial flexibilities are as follows:

- 1) Capital Receipts Received - dispensation for both 2020/21 and 2021/22 through Statutory Guidance to allow Councils to place capital receipts in the Capital Grants and Receipts Unapplied Account and then used to finance Covid expenditure (revenue).
- 2) Credit Arrangements (eg PFI / PPP Schemes) - at present Councils are required by statutory guidance to charge the debt element of service concession arrangements to their accounts over the contract period. A change to the accounting treatment will allow the debt to be repaid over the life of the asset rather than the contract period, applying proper accounting practices. Councils will have the flexibility to apply this change in either 2020/21 or 2021/22. This approach will apply to all credit arrangements going forward.
- 3) Loans Fund Principal Repayment Holiday - the flexibility being offered is a loans fund repayment holiday which will permit a Council to defer loans fund repayments due to be repaid in either 2020/21 or 2021/22 (but not both).

Discussions between Councils and the Scottish Government are on-going regarding the detailed operation of these flexibilities, particularly item 2 above. Final details will be issued by the Scottish Government in the form of Statutory Guidance and a change in Statutory Regulations. Recommendations will be presented to elected members in due course.

## 7.0 LOCAL GOVERNMENT FINANCE TRENDS 2013 – 2021

7.1 In June 2020, the Scottish Parliament Information Centre (SPICe) published its annual “Local Government Finance: Facts and Figures” report, covering the period 2013/14 to 2020/21. In terms of Local Government in Scotland as a whole, the key findings from the report include:

- Whilst the local government revenue settlement fell quite steeply in 2016/17, with smaller reductions 2017/18 and 2018/19, this trend now appears to be reversing.
- When comparing revenue settlements, real terms change figures show that between 2013/14 and 2019/20, the local government revenue settlement decreased at a faster rate (-4.7% or -£518 million) than the Scottish Government revenue budget (-2.2% or -£685 million).
- However, the trend is reversed when looking at the Local Government Finance Order figures for 2019/20 to 2020/21 - here the revenue settlement for local government increases by 3.8%, and the Scottish Government's revenue budget increases by 0.9%.
- From 2013/14 onwards the gap between changes to the Scottish Government revenue budget and the local government revenue budget became increasingly wide, reaching a peak in 2017/18 (6.4 percentage points). Over the last two years of outturn figures, this gap has narrowed, but overall the local government revenue budget has still fallen at a steeper rate than the Scottish Government revenue budget (2.5 percentage points difference between 2013/14 and 2019/20). This is due in part because of increased protection of the Health budget.
- The local government revenue settlement as a proportion of the Scottish Government revenue budget decreased by 2.6 percentage points between 2013/14 and 2019/20. Local Government Finance Order figures show Local Government revenue as a proportion of Scottish Government revenue increasing between 2018/19 and 2019/20.
- To provide some longer-term context, the briefing sets out ring-fenced funds as a proportion of total revenue settlement, between 2013/14 and 2020/21. There are increases shown across all local authorities, ranging from 3.4 percentage points to 10.2 percentage points.
- Local government funding per head of population has reduced for most Councils between 2013/14 and 2020/21, with reductions ranging from £29 to £250 for mainland Councils.

(Note: 1. All figures are expressed in real terms. 2. At the time of publication, the impacts and full funding picture relating to the Covid-19 response were still unfolding)

These figures again illustrate the financial challenges that local government in Scotland has faced in recent years.

## 8.0 BUDGET SAVINGS REQUIREMENT

8.1 As stated in paragraph 4.2 above, it is currently estimated that the Council requires to identify budget savings totalling £7.5m in order to set a balanced budget for 2021/22. This is based on the key assumptions included in the Council's 10-year revenue budget projections covering the period 2020-2030. These key assumptions include a flat-cash grant settlement and a 2% pay award and any movement against these assumptions will have a significant impact on the budget savings requirement. This is illustrated in the following table which highlights the savings requirement for 2021/22 based on different scenarios for the grant settlement and the pay award. The current planning assumptions are highlighted.

**Table 3: Budget Savings Requirement 2021/22**

	Grant Settlement 2021/22 (% Change from 2020/21)			
	0%	-1%	-2%	-3%
Pay Award 2021/22				
1%	£ 5.3 m	£ 8.2 m	£ 11.3 m	£ 14.2 m
2%	£ 7.5 m	£ 10.5 m	£ 13.5 m	£ 16.4 m
3%	£ 9.7 m	£ 12.7 m	£ 15.7 m	£ 18.6 m

Whilst the above figures represent a reasonable range of scenarios for the grant settlement and pay award, there can be no guarantee at this stage that the actual figures will fall within these ranges. In particular, there is considered to be a down-side risk around the grant settlement assumptions. In the 2020/21 grant settlement, the Council suffered a significant reduction in grant due to reducing support for loan charges and the impact of distribution changes. These reductions were, however, largely offset by the operation of the floor mechanism which limited grant losses to 0.44%. In the forthcoming 2021/22 grant settlement, the Council will again suffer a significant reduction in grant due to reducing support for loan charges and may also lose out due to the impact of distribution changes. At this stage, it is being assumed that these reductions will again be largely offset by the floor mechanism.

8.2 The figures in paragraph 8.1 above do not include any allowance for the additional income that would be generated by an increase in the Council Tax. A 1% increase in the current Council Tax level would generate net additional income of around £0.550m. It should be noted that, as part of the 2020/21 local government finance settlement, Councils had the flexibility to increase Council Tax levels up to a maximum of 4.84% in 2020/21 (3% in real terms). It is anticipated that a cap on Council Tax increases will again apply in 2021/22.

8.3 As detailed in paragraph 6.2 above, the Council is incurring a significant amount of additional costs in the current financial year related to Covid-19, including reduced income streams in many areas. Some of these cost pressures will continue beyond the end of the current financial year and into 2021/22, and possibly even beyond. Specifically, it is anticipated that shortfalls in some income streams (eg car parking, building control, trade waste collection etc) will not recover fully in the short to medium term due to the continuing economic downturn and new ways of working post-Covid 19 (eg more homeworking). This is a particular concern for Leisure and Culture Dundee, where it is anticipated that an income shortfall may occur across several financial years. The figures in paragraph 8.1 above do not include any allowance for additional costs relating to Covid-19. Whilst it is anticipated that the Scottish Government will continue to provide some level of additional grant support, it is likely that a budget deficit will arise due to Covid-19. At this point, it is being assumed that this deficit will be funded by applying one or more of the financial flexibilities set out in paragraph 6.3 above. This is an area that will be kept under constant review as the budget process progresses. It is emphasised that the financial flexibilities set out in paragraph 6.3 are only available over the

2020/21 and 2021/22 financial years. Accordingly, it may be necessary to identify savings in later years revenue budgets in order to fund any on-going cost pressures related to Covid-19.

- 8.4 The figures in paragraph 8.1 above do not include any allowance for additional costs relating to Brexit. Again, this is an area that will be kept under constant review as the budget process progresses.

## 9.0 LONG-TERM FINANCIAL STRATEGY

- 9.1 The long-term financial outlook and financial strategy for 2020 to 2030 were set out in Report 274-2019, which was submitted to the Policy & Resources Committee on 19 August 2019 (article XII refers). The approved long-term financial strategy, as set out in Report 274-2019, is as follows:

- the Council's corporate approach to identifying savings and efficiencies will be coordinated through the Changing for the Future transformational change programme (C2022) as agreed by Committee on 25 June 2018 (Article V of the minute of meeting of the Policy and Resources Committee of 25 June 2018, Report 223-2018 refers).
- the Organisational Change Fund, together with any capital receipts set aside to fund costs associated with future transformation projects, will help support and resource, on a spend-to-save basis, the organisational transformation that will be needed to deliver the required savings and efficiencies. This may include costs associated with VERs / VRs however, if no balances are available, then the initial costs associated with VERs / VRs will normally be met from service revenue budgets. On-going staff costs savings from VERs / VRs will be reflected in service revenue budgets.
- the Council will set annual balanced budgets, taking on board the prevailing constraints e.g. limits on Council Tax increases, reducing grant settlements, unavailability of balances etc.
- the Council will seek to achieve an overall outturn position each year in line with or below budget.
- the minimum uncommitted element of the General Fund balance will be the lower of £7 million or 2% of budgeted revenue expenditure but, ideally, a higher level will be held for operational purposes.
- services will be expected to operate within the limits of their overall revenue budget allocation. Cost pressures which emerge in-year should, where possible, be accommodated within the relevant service revenue budgets. The General Contingency should normally be used to fund items of a non-recurring or emergency nature. Expenditure of a recurring nature should normally be funded from within service revenue budgets.
- allocation of resources will be informed by a thematic approach designed to reflect the strategic priorities of the Council.
- budget provision will be made for estimated pay awards and, in limited circumstances, for areas of specific price inflation. The costs of incremental progression for staff will be funded from service revenue budgets.
- demographic growth will not be funded given the scale of the financial challenge. All services are expected to redesign services and work in partnership with other bodies to meet the cost of additional pressures.
- the reduction of grant that the Council receives after providing for new responsibilities will be shared by all directly provided and commissioned services, including Health and Social Care, Leisure & Culture Dundee and the Third Sector.

- Council Tax levels are planned to be increased by at least 3% per annum, but annual increases may be higher if allowed under the terms of the local government finance settlement.
- a review of resources within the Council will be undertaken to look at ways to deliver services more efficiently and effectively. Given employee costs currently account for around 65% of the net revenue budget, there is likely to be a significant reduction in the workforce of the Council.
- the Council's Capital Plan will be prudent, sustainable and affordable. In particular, affordability will be assessed with reference to the level of loan charges and additional running costs (including lifecycle maintenance) that can be reasonably included within future revenue budgets.
- the Council's immediate planning horizon for revenue expenditure will be three years and a rolling three-year revenue budget will be prepared annually and submitted to the Policy & Resources Committee as part of the budget approval process. In addition, projections covering a rolling ten-year period will be maintained and submitted, as necessary, to the Policy & Resources Committee.
- proposals for service re-design and service development will be underpinned by a comprehensive and robust business case, including options appraisal.

9.2 As noted in paragraph 8.3 above, it is currently being assumed that the budget deficit associated with Covid-19 will be funded by applying one or more of the financial flexibilities set out in paragraph 6.3. It is proposed that this arrangement should be included in the long-term financial strategy.

## 10.0 THE WAY FORWARD

10.1 The next key budget milestone for the Council will be the Scottish Budget announcements, expected on 28 January 2021. These announcements will include details of the Local Government Finance Settlement. The settlement will cover 2021/22 only, with little or no detail expected around future funding levels beyond then. The Scottish Parliament's budget scrutiny and approval processes will take place throughout February and into early-March, although there is, as yet, no detailed parliamentary timetable for the Budget Bill legislation.

10.2 A report will be submitted to the Policy and Resources Committee on 22 February 2021, detailing the Council's grant settlement for 2021/22 and the associated implications. This report will also include the proposed procedure for setting the Council's Revenue Budget and Council Tax for 2021/22. It is anticipated that the Policy and Resources Committee will meet on 4 March 2021 to set the Council's 2021/22 Revenue Budget and Council Tax.

## 11.0 LOOKING TO THE LONGER TERM

11.1 The national response to the Covid-19 epidemic has seen the UK Government incur unprecedented levels of expenditure, both in terms of measures to contain and fight the spread of the virus and to deal with the impact on the economy. The devastating economic impact has seen a record fall in GDP levels, leading to significant reductions in taxation revenues which in turn has necessitated record levels of government borrowing. This position is clearly unsustainable into the medium / longer term, where the resultant level of government debt will require to be addressed and managed down. This will be an enormous challenge for the public finances and is likely to have significant implications for the levels of government grant support that are available to Councils. This will be at a time when vital Council services will be required to deal with the social and economic aftermath of the epidemic, and when other sources of income available to Councils will be under severe pressure. The Council's longer-term financial projections and strategies will require to be revisited and updated to reflect the post-Covid situation and reports will be brought forward to the Policy and Resources Committee once more clarity emerges.

## 12.0 CONCLUSION

12.1 The Council is facing a significant challenge to deliver a balanced budget in 2021/22, against a back-drop of significant risk and uncertainty around the continuing impact of Covid-19, Brexit, government grant support and pay awards. There is a real risk that the actual grant reductions could be more severe than those currently being assumed.

13.0 **POLICY IMPLICATIONS**

13.1 This Report has been screened for any policy implications in respect of Sustainability, Strategic Environmental Assessment, Anti-Poverty, Equality Impact Assessment and Risk Management. There is a real risk that the actual grant reductions could be more severe than those currently being assumed.

14.0 **CONSULTATION**

14.1 The Council Management Team have been consulted on the content of this report.

15.0 **BACKGROUND PAPERS**

15.1 None.

**GREGORY COLGAN**  
**CHIEF EXECUTIVE**

**14 JANUARY 2021**