Agenda Item	3
Report No	HC/41/24

The Highland Council

Committee: **Highland Council**

Date: **12 December 2024**

Report Title: **Medium Term Financial Plan: 2025/26 – 2027/28**

Report By: **Chief Officer – Corporate Finance**

1. Purpose/Executive Summary

1.1 This report provides further update regarding the review and refresh of the Council's Medium-Term Financial Plan (MTFP) covering the three financial years 2025/26 to 2027/28.

1.2 This report supports the Council in its budget planning, and sets out relevant information, actions being progressed, and key next steps in support of the Council's budget plans and leading up to the formal setting of the 2025/26 revenue budget and council tax scheduled for the 6 March 2025 Council.

1.3 A particular focus in this report relates to the UK Government Budget of 30th October and in turn the scheduled 4th December Scottish Government Budget and resulting Local Government Finance circular, aspects of which (due to timing) will be by way of a supplementary update to this paper. Understanding of the impact of these Governmental budgets are key elements to inform the Council's budget planning and decision making.

1.4 The report also provides further update to members regarding a number of core aspects of financial planning, including: plans and strategies to address the projected budget gap, update on budget engagement arrangements, update regarding review of Council earmarked reserves, and finally this report sets out a draft suite of financial sustainability indicators which will form part of the report to Council in March 2025 and used as part of the Council's MTFP going forward.

1.5 This report also provides updated Highland Investment Plan (HIP) financial modelling, covering a 5-year capital planning horizon, to project out the capital funding envelope, and associated funding implications, to support member decision making on the Phase 1 HIP priorities covered by separate item on the agenda of this meeting.

2. Recommendations

2.1 Members are asked to:

i. Note the update provided relating to the UK Government Budget;
ii. Note the update provided relating to the 4th December Scottish Government Budget (to follow);
iii. Note the update relating to Medium-Term Financial Planning, the forecast budget gap, and actions and workstreams being taken forward;
iv. Note the update provided regarding review of Earmarked Reserves;
v. Agree to the re-allocation of re-purposed reserves into the Future Investment Capacity Fund;
vi. Note the update provided regarding the potential Highland Investment Plan (HIP) funding implications and Capital Quantum, and relevance to the separate HIP update provided on the agenda for this meeting;
vii. Note the update provided regarding Budget Engagement;
viii. Note the proposed draft Financial Sustainability Indicators with these to be updated and incorporated into the report to Special Council on 6th March 2025.

3. Implications

3.1 Resource - this report has a number of relevant resource implications as described within the report. The report, at this stage, is predominantly an update report and a report which progresses the review and updating of the Council's Medium-Term Financial Plan. Any specific resource implications relating to budget decisions would be addressed in future reports where there are specific budget decisions for Members consideration. Within this report the only specific recommendation with a resource implication relates to the proposed re-purposing of Earmarked Reserves (section 7). This recommendation does not represent a spending commitment, and is a re-purposing/re-categorisation within the Earmarked Reserves total.

3.2 Legal - In terms of Section 93 of the Local Government Finance Act 1992 ('the 1992 Act') Members have a duty to set both Council Tax and therefore by implication the next year's budget before 11 March in any year. Section 93(4) of the 1992 Act states *"in calculating such part of the total estimated expenses to be incurred by a local authority as falls to be met out of council tax, account shall be taken of any means by which those expenses may otherwise be met or provided for"*. Therefore, Council is required to estimate how much income it will receive from grant allocations, what its expenditure might be, what other budgetary actions can be taken, before then agreeing the Council Tax rate to fund the difference. This process is commonly referred to as 'setting a balanced budget'. This report will support the Council in its financial planning and fulfilment of these legal requirements and formal consideration at its Special Council meeting of 6th March 2025.

3.3 Risk - There remains uncertainty regarding financial outlook and financial settlements for Local Government, pending publication of the Scottish Government Budget and in turn the Local Government Finance Circular. It is also the case that these will be single year positions for 2025/26 only, therefore leaving further uncertainty regarding year 2 and 3 of the Council's planning assumptions. Through this report, such risks are intended to be mitigated through prudent budget planning assumptions and the benefits of decisions already made in February 2024, and the multi-year planning approach. Given uncertainty over the outcome and impact of pending UK and Scottish Government budget announcements, there remains the risk the scenarios as shown in this report, may need revisited in light of those budget announcements. The proposed Financial Sustainability Indicators as set out within this report represent further adoption of best practice and enhancement of the Council's financial strategies, to further support risk management and financial sustainability.

3.4 Health and Safety (risks arising from changes to plant, equipment, process, or people) – no specific risks arising from this report.

3.5 Gaelic - no specific risks arising from this report.

4. Impacts

4.1 In Highland, all policies, strategies or service changes are subject to an integrated screening for impact for Equalities, Poverty and Human Rights, Children's Rights and Wellbeing, Climate Change, Islands and Mainland Rural Communities, and Data Protection. Where identified as required, a full impact assessment will be undertaken.

4.2 Considering impacts is a core part of the decision-making process and needs to inform the decision-making process. When taking any decision, Members must give due regard to the findings of any assessment.

4.3 This is a monitoring and/or update report and therefore an impact assessment is not required.

5. UK Government Budget / Scottish Budget

5.1 Members will recall from the MTFP report to the October 31st Council, that a verbal update was provided by the Section 95 Officer regarding the Chancellor's UK Budget the day before, the 30th October. Some of the key messages and subsequent analysis of that budget, as it relates to Scotland and Local Government, is set out in **appendix 1**. This is based on information sourced from UK Government, Scottish Government, CoSLA and external economic and other analysis.

5.2 The Scottish Budget is scheduled for issue on 4th December. It is intended that relevant information that arises from that publication will be issued as a supplementary briefing item to this report. **Appendix 2** of this report is a placeholder for that Scottish Government budget briefing, and will be circulated when available. It is likely it may be some days post-4th December before an update is issued, to give time for analysis and also receipt of other information from CoSLA and other sources. As is typically the case, it will be high level analysis and context, rather than detail specific to Highland that will be drawn from the Scottish Government budget analysis.

5.3 The Local Government Finance Circular is expected to be released the week following the Scottish Government Budget. It is this circular which will provide information on the Council's revenue and capital grant funding for 2025/26, and detailed information on how this has been calculated. The Council expects the circular to be released on 11th or 12th December. Given the amount of detail within, and sitting behind the circular, there is inevitably always some time following issue before the Council is in a position to analyse and assess implications. It may be after the Council meeting on the 12th December until information is available, or implications more clear.

5.4 It is currently understood that the final stage of the passing of the Scottish Government Budget, and the Local Government Finance (LGF) Order, which approves the grant funding to Councils, may be on or around 1st week March. Potentially therefore Parliament having formalised the grant funding settlement prior to the scheduled Special Council meeting on 6th March 2025. Were the timing of LGF Order to change, it is not without precedent for that Order to take place after budget/council tax setting day, and were this to be the case it would not prevent the Council making decisions on the 6th March.

6. Financial Outlook and Budget Planning

6.1 Pending receipt of information and analysis of the Scottish Government Budget and Finance Circular, the Council's planning assumptions remain those as at the report to October Council. Which are re-stated below.

	Current £m	Revised - Mid £m	Revised - Worse £m
Forecast Budget Gap - **BEFORE** Agreed Mitigations/Savings			
- 25/26	35.675	43.712	49.749
- 26/27	35.046	46.089	53.568
- 27/28	23.381	26.373	28.335
- 3 Years	94.102	116.174	131.652

The headline gap above, after allowing for existing approved budget savings, and current assumptions on council tax and reserves, is as follows. Formal decisions on council tax and reserves will of course be for the 6th March 2025 Council meeting.

	Current £m	Revised - Mid £m	Revised - Worse £m
Forecast Budget Gap - AFTER Mitigations/Savings/Funding assumptions			
- 25/26	0.710	8.747	14.784
- 26/27	-0.342	10.701	18.180
- 27/28	15.800	18.792	20.754
- 3 Years	16.168	38.240	53.718

6.2 As can be seen from the UK Budget briefing on **appendix 1**, while there appears to be an acknowledged increase to the Scottish Budget for 2025/26, and expected additional funding for National Insurance increases, there also appears to be an expectation from Scottish Government that the funding for National Insurance is less than their estimation of cost. An important matter is also that the implications of National Insurance increases are not only those relating to the Council's own workforce and pay bill. The cost of goods, services and contracts may all be impacted, with expectations or increases that may impact on the Council going forward. It is unclear, and potentially unlikely, that any funding recognition of National Insurance costs addresses in full the implications across both Council workforce and those wider impacts.

6.3 There may be some offsetting effect arising from the UK Government budget, i.e. the possibility (given a cash increase in SG Budget) that a Local Government settlement may be better than that assumed at October and in the forecast gaps as above, but that potentially offset by the risk that National Insurance costs are not fully funded. Until the release of Scottish Government budget, this is only speculation at this stage. On balance therefore, the forecast gap and planning assumptions at October 2024 remain reasonable assumptions. Were there to be an improvement, say, relative to the forecast, the benefits of a multi-year approach are that savings and other plans could be utilised in years 2 or 3, rather than year 1. Conversely, a multi-year approach can also support a bringing forward of future year savings and strategies, should there be a need to address a worse position than forecast.

6.4 There are a number of workstreams progressing to support the Council's Medium Term Financial Plan, with these including.

- Review of in year pressures and budget monitoring;
- Review of delivery of agreed budget savings;
- Consideration of pressures and risks relating to the budget;
- Review of reserves and earmarking (see next section);
- Identification of new/additional saving proposals and other strategies.

6.5 This work will support formal consideration of budget proposals by the Council on 6th March 2025. As previously stated, the approach is based upon a rolling three year Financial Plan covering 2025/26 to 2027/28.

6.6 In relation to pressures, work is taking place to identify budget pressure and risk areas for the three-year plan, and also any update or revision to new burdens and investment. Taking account of planning assumptions for 2025/26 – 2026/27 from the February 2024 report, and updated forecasts from the October 2024 report to Council, the current position is as shown below. The current focus is identification and assessment of pressures and risks. The extent to which these can be managed within, or ideally below the levels shown below, would help reduce or mitigate the budget gap.

Recurring budget pressures	2025/26	2026/27	2027/28
Assumptions at February '24	12.000	10.000	-
October '24 MTFP review and increase to manage risks	+8.000	+8.000	+12.000
Sub-total	20.000	18.000	12.000
Feb '24 indicative allocations: - PPP flexibility interest costs - Capital investment (Roads/Corran Ferry Infra) - Capital multiplier	 -1.023 -1.000 -3.000	 -0.909 -1.000 -5.000	 - - -
Unallocated / Balance	14.977	11.091	12.000

6.7 The types and category of risk and pressure that may need considered in the budget, and seen in the context of the assumptions above, are as follows.

- Inflation and related pressures (£7.8m was allocated for this purpose alone in 24/25);
- Pay award risks;
- National Insurance paybill costs (if not fully funded). HC estimated cost c£9m;

- National Insurance – wider impact on costs of goods and services;
- Other demand led pressures, new burdens and priorities;
- Risks around savings delivery;

6.7 Savings and other financial strategies will be necessary to address the budget gap. It is expected that similar themes and workstreams to those which formed the current approved £54.6m package of savings, will be a focus for member decision making on the 6th March 2025. That does not however preclude new or additional themes or proposals being considered. The scale of the budget gap, and impact of Local Government Finance settlement, once known, will ultimately be a key factor in both the scale and impact of savings required. Given the pressure on public sector finances, despite the Council's focus to date on income generation, change and transformation, budget savings and service reductions will also need considered.

7. Earmarked Reserves

7.1 The Council has an agreed Reserves Strategy, and based on budget and other decisions has earmarked significant sums into reserves for specific purposes, including to support investment, change and transformation. The following summarises the current position regarding Earmarked Reserves. Note that by year end there would be an expected decrease in some values shown to reflect the drawdown and use of reserves for agreed purposes.

	£m
Total Earmarking at Start of Year	£110.779m
Of which: - Subject to contractual, external or other controls or requirements. - New February 2024 MTFP earmarking - Residual legacy earmarked reserves	 £28.554m £58.407m £23.818m

7.2 There has been an ongoing officer review since budget decisions in February 2024, recognising that some elements of the earmarked reserves dated back some years and to past budget decisions, and given the passage of time there was a need to review. In particular to consider what was the original purpose of the sum earmarked, what had been drawn down to date, what outcomes had been delivered or concluded, whether any outstanding deliverables remained, how the reserve related to current priorities, and whether the passage of time had altered the funding need or had other funding sources become available. The extent to which existing earmarking could be re-purposed could support the Council in relation to current priorities and opportunities.

7.3 Some earmarked reserves, by their nature, the Council has limited or reduced scope to review or re-purpose. This includes those reserves which are covered by legislation/regulation/direction (e.g. schools DSM reserves), contractual arrangements (e.g. S75/Developer contributions), external funding and direction (e.g. external grant or match funding held in reserves). While these reserves have been considered in review, no re-purposing or re-allocation is possible or proposed. The new earmarking agreed as part of the February 2024 budget decisions and MTFP have also been considered but no review or re-purpose proposed at this stage, given the relatively recent decision making relating to them. The focus therefore has been those remaining earmarked reserves Council has discretion in, and many of which are legacy reserves and related to part budget years, to identify scope to re-purpose reserves. In total, the outcome of this exercise has been £4.513m identified and proposed for re-allocation to the existing 'Future Investment Capacity Fund'. Further details regarding the £4.5m are enclosed as **appendix 3**.

That would result in that Fund within earmarked reserves totalling £13.932m of which £3.466m is committed based on decisions by the Council relating to resourcing of the Operational Delivery Plan.

No specific use cases or commitments are outlined in this report.

Of the remaining £10.466m that would represent capacity for the Council to utilise to fund other priorities and commitments, some of which are investment or expenditure proposals covered by recent of other separate papers on this Council agenda.

7.5 Further analysis of, and recommendations relating to reserves, will form part of the budget report to be considered by the Special Council meeting of 6th March 2025.

8. Highland Investment Plan – Funding and Capital Quantum

8.1 Members will recall the core financial and funding principles which underpin the Highland Investment Plan (HIP) and were considered in detail as part of the May 2024 report to Council. The financial modelling reflected within that report was a long-term 20-year projection, and to inform decisions to be made by members at this meeting, an updated 5-year profile, using the same core financial principles, has been set out within this report as follows.

TABLE 1: Projection of revenue value of 2% earmarked to support HIP borrowing

	24/25 £m	25/26 £m	26/27 £m	27/28 £m	28/29 £m	29/30 £m
A : Baseline assumption of 5% Council Tax Rate Increase + 2% for HIP	2.800	3.050	3.289	3.554	3.841	4.150
B: Modelling of 1% Lower baseline increase	2.800	3.050	3.257	3.488	3.733	3.996
C: Modelling of 1% Higher baseline increase	2.800	3.050	3.319	3.622	3.950	4.308

These sums being the revenue which could be earmarked into revenue loan charge budgets to meet future borrowing costs, and support HIP capital investment.

TABLE 2: Indicative capital quantum as a result of the revenue projection above.

	2024/25 Current Year £m	Next 5 Years £m	5 Years plus Current £m
Baseline 5%+2%	46.200	295.077	341.277
+1%	46.200	301.079	347.279
-1%	46.200	283.890	330.090

The capital quantum is also reflected within the separate HIP report on this agenda and with further commentary and context regarding the capital and investment considerations.

8.2 This provides an indication of the potential capital funding quantum that could be available to the HIP over the forthcoming 5-year period. This is subject to revenue budget and council tax decisions to be made by Members on an annual basis. This quantum is based on the following underlying assumptions.

- Multi-year funding models will support decision making over the medium to long-term, recognising that capital investment decisions are multi-year and long-term commitments.

- A revenue budget sum equivalent to 2% of council tax p.a., will need to be created and earmarked to support the HIP year on year. This will create a year on year and stepped increase in revenue funding to support the HIP.

- Council tax as a funding source provides a foundation for that 2% to rise in value year on year (as the base on which it is calculated rises) and represents a mechanism which will increase the overall revenue funding for the Council which can support capital.

- It is however the case, as per the May 2024 report, that other funding streams could be considered as a means to secure a sum equivalent to the 2%.

- The base level of council tax on which this earmarked sum will be based, will vary depending on factors such as the overall level of council tax charge each year, and the number of properties to which it applies. Both of these are variables, and this report is based on the following assumptions:

    - A core council tax increase of 5% p.a., with the HIP earmarking of 2% being over and above this baseline.
    - An illustration of the effect of each 1% +/- on that baseline.
    - An assumed year on year increase in the tax base (number of properties) based on trend data.
    - Any change to these assumptions, up or down, would alter the base on which the 2% is calculated, and therefore increase or decrease the investment quantum available.

- The revenue funding realised from the 2% earmarking, would be added to the Loan Charge revenue budget, which meets the cost of repaying debt/capital investment.

- That increase in revenue loan charge provision, which will year on year increase that budget, will provide the capacity for a capital investment quantum to meet HIP priorities.

- The level of capital capacity will depend on the HIP priorities and projects agreed, given loan charges are linked to the expected useful life of the asset. Interest rates will also impact with modelling based on current average loans fund interest rates.

- This report is based on average/typical levels of capital quantum based on historic capital spend and based primarily on schools/properties/roads being the expected likely investment priorities from within the HIP.

- The actual capital quantum will need to be re-assessed in light of future decisions on specific projects, costs and spend profiles, and prevailing interest rates, which may in turn require a re-profile of capital project plans to align.

- There will, in parallel to the HIP quantum met from the earmarked 2%, be a core capital investment programme to meet other capital needs and priorities (including fleet, ICT, flooding, waste, bridges, etc), and associated loan charge commitments which will also form part of the Council's financial planning and annual budget decision making.

8.3 Council tax and budget decisions are of course taken on an annual basis. The figures within this report are to provide an indication of the potential capital quantum. It will be the March 2025 Special Council meeting where the Council will formally make its budget and council tax decisions for 2025/26, in turn creating and earmarking funds to provide some of the initial HIP capacity.

8.4 Given capital investment is multi-year and results in longer-term commitments, it is important that Members understand that a single year earmarking of HIP revenue funding will only result in a single circa £50-60m of capital quantum, with that revenue funding then repaying debt over the longer-term (typically over 30 years or more). Given this report is focused on an initial 5-year phase of the HIP, and much larger scale investment over that period, investment priorities will require the Council to make year on year revenue funding commitments to create new and additional 2% earmarking to support the HIP each year. HIP decisions now and in the coming months will potentially forward commit the Council in terms of revenue budget implications over the medium-term.

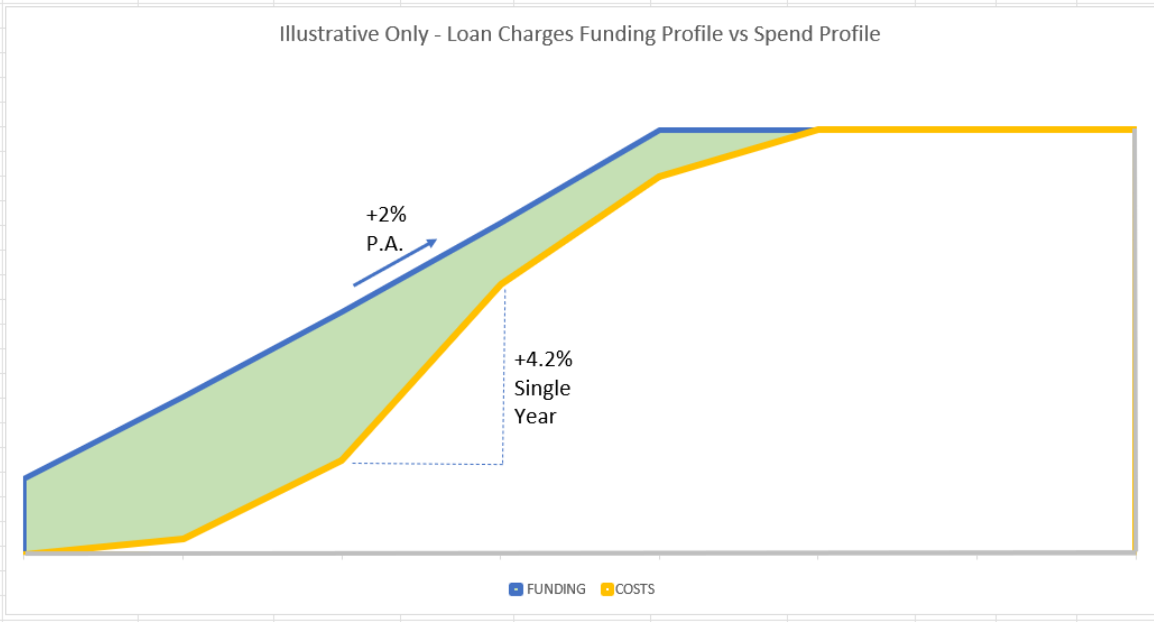
8.5 There will be an inevitable time lag between the revenue funding earmarked and the spending of capital on HIP priorities. Moreso in this initial phase of the HIP and recognising there is a lead time between engagement and project development, before significant on the ground expenditure. A short to medium-term underspend on loan charges can therefore be expected. Over time, and as future phases of the HIP are decided upon, and on the ground capital investment ramps up, any underspend would be expected to reduce and taper out.

8.6 Further modelling of the loan charge profile will be undertaken, and consideration given to any further strategies to align with the HIP, where any short-term loan charge underspend could, for example, support other Council priorities.

8.7 The revenue budget created will ultimately be required to meet the long-term capital repayment implications. A fundamental principle of the HIP funding model agreed in May 2024 was the need to ensure revenue budget decisions and earmarking of funding was agreed ahead of the allocation of funds – to protect the funding and affordability of the HIP.

8.8 Purely as an illustration, the graph below gives a contrast of a potential HIP funding profile contrasted with a capital spend/loan charges profile. This **is not** modelled on specific Highland priorities or spend profiles, given they have still to be determined, and is purely used for illustration. It gives a visual representation showing how a short to medium term underspend (the green area) might be expected, but importantly, also shows that over the long-term, there should be alignment between budget funding and actual loan charge costs and the HIP funding strategy is designed such that long-term funding implications can and are provided for based on member decisions.

8.9 The agreed HIP funding approach provides a steady, planned and predictable build-up of revenue to provide for the loan charge budget (the straight line). This avoids more volatile year on year funding requirements, significant funding pressures in particular years, and scenarios which may compromise the ability to annually provide for revenue budget implications. Using the illustration below, rather than a steady 2% p.a. build-up of funding for capital, the alternative would be more volatile and more significant funding pressures in a single year e.g. 4.2% in the illustration below (and this being over and above all other funding needs). This graph demonstrates the benefit of the principles agreed for the HIP, and the steady build-up of funding to support the HIP.



9. Budget Engagement

9.1 The current programme of activity builds on the feedback received during the 2024/25 Budget Challenge approach. With over 3,500 responses received, this shaped both the budget proposals and the Council's Delivery Plan. The budget setting process will therefore continue to review and take account of the feedback received during last year's engagement process whilst seeking further ideas and views for 2025/26.

9.2 Our Future Highland 2025/26, updates the public on what feedback was received, how that shaped the proposals that came forward and the work that is in place to deliver this. Whilst acknowledging the service redesign and income generation proposals that have been progressed, it also highlights the investment that has been committed to through the Highland Investment Plan.

9.3 This year's budget engagement will begin on the week of the 2nd December 2024. It will run until Monday 20th January. The Council's Engagement HQ site will again be utilised and host both a survey asking for ideas and suggestions in relation to the 4 Budget Themes of:

- Redesigning our services
- Changing how we manage our buildings
- Generating more income
- Being more efficient in how we do things

We will also utilise an Ideas Board which proved successful last year in generating ideas from the public in how we generate income or changing what we do.

9.4 Beyond the online engagement, budget engagement materials will be available in service points and libraries and shared with key groups and community partners for feedback. As part of the budget setting approach, engagement with partners will also be key in developing and aligning our local priorities.

10. Financial Sustainability Indicators

10.1 The Council already maintains a range of indicators which measure financial performance and sustainability, and there are other routine and regular financial reporting arrangements to members on a breadth of financial matters. There is however a case for consolidating this activity into a Financial Sustainability Toolkit, to support the Council and elected member decision making.

10.2 This report sets out background, and a proposed suite of Financial Sustainability Indicators, that will be developed and used going forward. In particular, the indicators will be considered by Council as part of the annual budget and council tax setting process each year, and will be used to inform the requirement for the Section 95 Officer to comment on the financial sustainability of the Council on an annual basis.

10.3 The purpose of this report is to introduce the draft Indicators, with these then being reported to Members at the Special Council meeting of 6th March 2025. Ongoing monitoring through the year would be expected to be through a combination of incorporation into existing reports to Council and/or Corporate Resources Committee. A number of the indicators are already monitored in this way, but would now be formally consolidated into the suite of Financial Sustainability Indicators.

10.4 The driver behind the approach described is as follows. The Council has already adopted and complies with the Cipfa Financial Management (FM) Code, the Prudential Code for Capital Finance, and the Treasury Management Code of Practice amongst others. It has also developed its internal process and strategies over recent years, for example through the agreement of a Reserves Strategy, the adopting of a Medium-Term Financial Planning approach, and development of a longer term approach to capital through the Highland Investment Plan. It is clear however there would be benefits in consolidating some of the key indicators and performance measures which sit within these existing plans, strategies and reports, into a single suite of Financial Sustainability Indicators. That would not replace those existing reports, rather compliment them and give a single and focused view on those most significant measures of financial sustainability. Doing to would also support the Council in adopting and demonstrating best practice, considering External Audit and Accounts Commission interest and expectations in this area.

10.5 A draft list of Financial Sustainability Indicators is attached as **appendix 4**. This is provided for illustration at this time, with further work to develop and potentially add to the Indicators before they are incorporated within the budget report to Council on 6th March 2025.

Designation: Chief Officer, Corporate Finance

Date: 29 November 2024

Author: Brian Porter, Chief Officer – Corporate Finance

Background Papers:

Appendices: Appendix 1 – Briefing on UK Government Budget
Appemdix 2 - Placeholder for Briefing on Scottish Government budget
Appendix 3 – Earmarked Reserves Re-purposing
Appendix 4 – Financial Sustainability Indicators

Appendix 1

Briefing on UK Government Budget of 30th October 2024

Sources: UK Government/HM Treasury, Scottish Government, Cosla, Cipfa Director of Finance Section economic advisor, Press Briefings and other Information.

<u>Key Points:</u>

<u>Scotland</u>

- The Scottish Government is stated as receiving £47.7 billion in 2025-26, including an additional £3.4 billion through the operation of the Barnett formula. Of this £2.8 billion resource (revenue) and £610 million capital funds.

- Current understanding via Scottish Government/Cosla of the Barnett consequentials:

    - The UK Budget contained a cumulative £3.4 billion of Barnett consequentials for the Scottish Government, around £1.5 billion for 2024-25 and around £2.0 billion in 2025-26 in cash terms.
    - In 2025-26, the Scottish Government's Resource Block Grant will increase by around £1.4 billion (around 3.4%) in cash terms relative to 2024-25.
    - Controlling for inflation, this is a real term increase of around £400 million (or 1.0%).
    - In 2025-26, the Scottish Government's Capital Block Grant will increase by just under £700 million (around 12.3%) in cash terms relative to 2024-25.
    - In real terms this is an increase of around £600 million (10.2%).
    -

<u>National Insurance</u>

- Firms to pay National Insurance on workers' earnings above £5,000 from April, down from £9,100 currently, with the rate increasing from 13.8% to 15%

- Employment allowance - which allows companies to reduce their NI liability - to increase from £5,000 to £10,500 (applies to smaller organisations only)

- An initial Scottish Government estimate of the cost to the public sector in Scotland is around £500 million in 2025-26. Funding for this change has not yet been included in the Scottish Government Resource Block Grant for 2025-26. HM Treasury have confirmed that an exercise will be run to calculate costs for the public sector and further funding will be provided at UK Main Estimate in Spring 2025.

- Recent press coverage has suggested the NI funding allocation to Scotland may be in the region of £300m (contrasted with the £500m Scottish Government estimate).

- A further impact and consideration is the impact on business and 3rd sector, which may lead to further implications beyond the direct cost on the public sector paybill.

UK debt, inflation and economic growth

- Office for Budget Responsibility predicts the UK economy will grow by 1.1% this year, 2% next year, and 1.8% in 2026

- Inflation predicted to average 2.5% this year, 2.6% next year, before falling to 2.3% in 2026

- Official definition of UK government debt loosened by including a wider range of financial assets, such as future student loan repayments

Shared Prosperity

- Continuing the UK Shared Prosperity Fund at a reduced level for a further year, providing £900 million; this transitional arrangement will allow local authorities to invest in local growth, in advance of wider funding reforms.

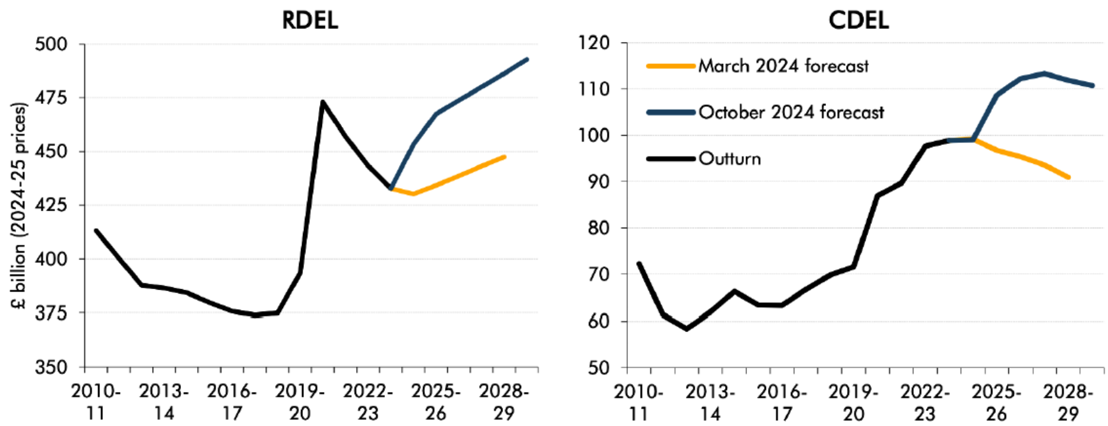
- The government will reform the local growth funding landscape at Phase 2 of the Spending Review: rationalising the number of funds, moving away from competitions, and better supporting local leaders to drive growth. The government will also set out more detail on its strategy for regional growth alongside, and integrated with, plans for infrastructure, investment, and the Industrial Strategy

Longer-term Outlook

The UK Budget did not set out Departmental spending budgets post 2025-26. However, it did outline the spending envelope up to 2029-30 on which these budgets will be based at the time of the UK Spending Review (SR), next Spring.

Sourced from that UK Budget data, the graphs below show that for both resource (day-to-day spending) and capital budgets, the funding envelope is higher in real-terms against last March's UK forecast. There is however a 'slowing down/tailing off' beyond 2025/26.

Figure 1: Real terms, total, departmental resource and capital budget envelope



Source: HM Treasury, OBR

Appendix 2

Supplementary annex to item 3. Medium Term Financial Plan: 2025/26 – 2027/28

Scottish Government Budget 2025/26

Introduction

This briefing provides some initial analysis and commentary regarding the Scottish Government Budget 25/26 as published 4th December. It draws on supplementary information and briefings provided to officers by Cosla and Scottish Government.

More analysis, and supplementary information may be provided to Councils in the coming days, and any material points will be provided by way of verbal update on 12th December. At this stage this briefing does not draw any specific conclusions or make commentary regarding implications for the Council's financial plans given more detailed consideration and further information is required to do so.

It is important to note the Draft status of the Scottish Government budget, and that the individual draft grant settlements for Councils will only be released on or around 11/12th December, and that will ultimately be the information which gives a clearer position in terms of budget implications for the Council.

Local Government – Key Headlines and Analysis

- No council tax freeze or cap but expectation that any proposed increases are minimised.

	Revenue £m	Capital £m	Total £m
Funding announced for 25/26	14,258.1	777.1	15,035.2
Funding provided for 24/25 *	13,389.1	638.0	14,027.1
Cash increase as presented in Scottish Budget	869.0	139.1	1,008.1
Initial Analysis of Cash Increase			
Funding to meet existing commitments including 24/25 pay, pension and other commitments	308.6	31.0	339.6
New or additional funding but with some direction, expectation or new burdens (spending) associated.	271.1	60.0	331.1
New and additional funding but with no specific direction associated. General Revenue Grant. Equates to approx. +2.2% cash increase.	289.3	48.1	337.4
Total	869.0	139.1	1,008.1

* Being Finance circular 8/23 + £144m Council Tax Freeze for 24/25

- Further detail and analysis of new burdens, expectations and direction associated with some of the additional funding will be required. With expectation further communications from Scottish Government are received in coming days and weeks. The new/additional funding above relates to matters including: maintaining teacher numbers, ASN and adult social care, Real Living Wage costs, Free school meals, climate change (capital) and play parks (capital).

Other Key Points

- £768m investment in affordable homes, enabling over 8,000 new properties with social rent, mid-market rent and low-cost home ownership to be built or acquired this coming year
- £21bn for health and social care
- Restore a universal winter heating payment to every pensioner household
- £25m to support the creation of new jobs in the green energy supply chain
- £3 million for a Bright Start Breakfasts pilot
- £300m will be invested in upgrading heating and insulation to homes and workplaces
- £90m to protect, maintain and increase Scotland's woodlands and peatlands
- Almost £190m to help people to walk, wheel or cycle, and invest in resilient, efficient bus services
- £150m investment in offshore wind
- £1bn to deliver "efficient and resilient roads", including money to complete the dualling of the A9
- £34m investment in culture sector this year with a further increase of £20m next year and also non-domestic rates support for music venues
- No new bands or increase the rates of Scottish income tax for the remainder of this parliament but basic and intermediate rate thresholds will increase this year by 3.5%
- Two-child benefit cap will be scrapped by 2026

Earmarked Reserves - List for Re-purposing

Earmarked Balance	Earmarked Balance at Start of Year £	Proposed Amount for Re-allocation to the 'Future Investment Capacity Fund' £	Comments
Badaguish Outdoor Centre	459,692	**459,692**	Earmarking no longer required following review
Business Change & Improvement - Transformation Fund Reserve	1,012,858	**852,858**	Balance after commitments of £160k no longer required due to new earmarking at the 23/24 year end for Delivery Plan investment
Covid-19 & Welfare	601,941	**591,070**	Uncommitted balance, after drawdown of £11k for last post funded from LACER funding. Any further commitments or needs met from existing revenue budget/funding.
Education Transitional Funding	1,205,588	**700,000**	£0.7m of this balance is no longer required due to the work currently being carried out to rebase the Education budget. £0.5m will be required to support the Workforce for the Future Portfolio and to support further service improvement.
HLH Review	100,000	**43,157**	Balance after meeting costs of external support for the review.
Learning & Teaching (1+2 Languages)	99,200	**99,200**	Balance no longer required as any costs met from existing budget/funding.
Mental Health Officers	139,000	**139,000**	Balance no longer required as any costs met from existing budget/funding.
Period Poverty	96,751	**96,751**	Outcomes being met by existing revenue budget/funding.
Phase 1 Investment Fund - Visitor Management Strategy	318,759	**311,963**	Balance, after £7k transfer to Phase 3 Investment Fund. There is also £102k retained in Phase 3 Investment Fund balance for committed Visitor Management projects.
Phase 2 Investment Fund - Environment/Climate Change - Renewables	100,000	**100,000**	No longer required due to new earmarking at the 23/24 year end for Delivery Plan investment.
Phase 3 Investment Fund - Green Energy Hub	655,442	**455,000**	Long-term Waste Management strategy confirmed by C&P Committee on 27 Nov 2024 removes the requirement for this earmarking.
Phase 4 Investment Fund - Innovation in Education	295,385	**295,385**	Posts funded by this reserve will be met from recurring revenue budget following the Education re-structure
Staffing Conditions & Development Fund - Consolidation of Living Wage	342,481	**342,481**	Balance no longer required - ongoing cost of consolidation of living wage met from recurring revenue budget.
Website & Service Centre Enhancement	26,255	**26,255**	No longer required due to new earmarking at the 23/24 year end for Delivery Plan investment.
		4,512,812	

Appendix 4

Financial Sustainability Indicators (draft)

Plans and Strategies

Duration of Medium-Term Financial Plan/Strategy	(Years)
Status of the Plan/Strategy	(approved mm/yy)

Reserves

Council's Reserves Target	(% and £ target)
General (non-earmarked reserves) relative to target	(% and £ amount)
Total level of usable reserves	(£ amount)
3-year movement in reserves (past three financial years)	(£ amounts)

Savings and Delivery

Current 3 year MTFP Gross Forecast Budget Gap	(£ amount)
Agreed/Planned Mitigations/Measures to address the Gap	(£ amount)
Net Residual/Outstanding Budget Gap	(£ amount)
Ratio of Mitigations/Measures which are recurring/non-recurring	(% / %)

Budget Out-turn

Revenue out-turn as a % of Budgeted Expenditure (past 3 years)	(%, %, %)

Capital Investment and Borrowing

Total External Borrowing	(£ amount)
Total Capital Financing Requirement	(£ amount)
Ratio of financing costs to net revenue funding: (a) Including PPP/PFI costs (Prudential Indicator) (b) Excluding PPP/PFI costs (Local HIP Indicator)	 (% actual) (% target / % actual)