P.2023/101

THE STATES OF DELIBERATION
of the
ISLAND OF GUERNSEY

POLICY & RESOURCES COMMITTEE

FUNDING & INVESTMENT PLAN

The States are asked to decide:-

Whether, after consideration of the policy letter entitled 'Funding & Investment Plan' dated 11th September 2023, they are of the opinion:-

1. To agree that the financial position of the States requires urgent attention and that, as a bare minimum, the following core measures should be agreed which will temporarily stabilise the position:-

    a. implementing the package of core cost reduction targets and revenue raising measures set out in Appendix 1;

    b. maintaining the current level of the General Revenue Reserve in this term;

    c. investing up to £95m to complete the 'in flight' capital schemes as set out in Appendix 1; and

    d. investing in the policy, strategies and plans agreed as part of the Government Work Plan over the remainder of this term of government;

    and to authorise the Policy & Resources Committee to implement these agreed measures.

AND IF PROPOSITION 1 IS APPROVED:-

SCENARIO 3

2. To agree that the States shall address the current and future expected structural deficit and historical chronic under-investment in public infrastructure by way of the following measures:-

    a. implementing the full progressive tax and benefits package as proposed to the States in early 2023 (see item 5, entitled "The Tax Review: Phase 2, P.2022/112" on Billet d'État No. III of 2023 P.2022/112) and set out in Appendix 1, in order to put the finances of the States into a sustainable position thereby being able to afford future capital investment, address the deficit and begin to rebuild reserves;

    b. agreeing that the Policy & Resources Committee should work with Principal Committees to develop a plan for the use of ringfenced funds of £2.5m per annum for social and community benefit, as set out in Paragraph 8.2 of this policy letter;

c. adopting Portfolio 3 estimated at a total of £520m (including the in-flight schemes), as set out in Appendix 1, as the agreed major capital investment portfolio for the remainder of this term;

d. on the basis that funding available is insufficient to fund Portfolio 3, agreeing therefore that new borrowing should be taken out to support the funding of major capital expenditure; and

e. increasing the authority granted to the Policy & Resources Committee in Resolution 16[1] on item 1, entitled “Government Work Plan 2021-2025, 2021/71”, of Billet d’État No. XV dated 21st June 2021, to enable the Committee to take out new borrowing to a maximum of £350m;

and to authorise the Policy & Resources Committee to implement these agreed measures.

OR IF PROPOSITION 1 IS APPROVED BUT PROPOSITION 2 IS NOT APPROVED:-

SCENARIO 2

3. To agree that the States shall address historical chronic under-investment in public infrastructure by way of the following measures:-

    a. adopting Portfolio 2 estimated at £440m (including the in-flight schemes), as set out in Appendix 1, as the agreed major capital investment portfolio for the remainder of this term;

    b. on the basis that funding available is insufficient to fund Portfolio 2, agreeing therefore that new borrowing should be taken out to support the funding of capital expenditure and that the balance of the Health Service Reserve should be used to fund the Our Hospital Modernisation Programme; and

    c. reaffirming the authority granted to the Policy & Resources Committee in Resolution 16 on item 1, entitled “Government Work Plan 2021-2025, 2021/71”, of Billet d’État No. XV dated 21st June 2021, to take out new borrowing to a maximum of £200m;

    and to authorise the Policy & Resources Committee to implement these agreed measures and direct it to return to the States by September 2026 with proposals for addressing the deficit and putting the finances of the States into a sustainable position.

[1] This Resolution authorised the Policy & Resources Committee to take out new external borrowing up to a total maximum of £200million for a period of up to 40 years, on such terms and conditions as the Committee deem appropriate.

OR IF PROPOSITION 1 IS APPROVED BUT PROPOSITIONS 2 AND 3 ARE NOT APPROVED:-

SCENARIO 1

4. To agree that the States shall limit investment in public infrastructure to critical investment only until such time as measures are agreed to address the structural deficit and to:-

    a. adopt Portfolio 1 capped at £190m (including the in-flight schemes), as set out in Appendix 1, as the agreed capital investment portfolio for the remainder of this term;

    b. limit major capital expenditure to funds of £190m available from within existing reserves; and

    c. rescind Resolution 16 on item 1, entitled "Government Work Plan 2021-2025, 2021/71", of Billet d'État No XV dated 21st June 2021 authorising the Policy & Resources Committee to take out new borrowing to a maximum of £200m;

    and to authorise the Policy & Resources Committee to implement these agreed measures and direct it to return to the States by September 2026 with proposals for addressing the deficit and putting the finances of the States into a sustainable position.

AND, ONLY IF PROPOSITION 2 IS APPROVED TO AGREE

EITHER:

5. As part of the package of progressive measures as set out in Scenario 3 in Appendix 1, to introduce a broad-based Goods and Services Tax at a rate of 5%, as laid out in Section 8 of this policy letter, with minimal exemptions and zero rating.

OR:

6. As part of the package of progressive measures as set out in Scenario 3 in Appendix 1, to introduce a broad-based Goods and Services Tax at a rate of 6% with minimal exemptions and zero rating excepting that a zero rate should be applied to food and non-alcoholic drink products, as laid out in Section 8 of this policy letter.

AND IF PROPOSITION 5 OR 6 IS APPROVED

7. To agree that the legislation implementing the introduction of Goods and Services Tax shall come into force on 1 January 2026 and remain in force until 31 December 2032, unless extended for such periods as the States may by Resolution determine following recommendations by the Policy & Resources Committee.

AND

8. To direct the preparation of such legislation as may be necessary to give effect to the above decisions.

<u>THE STATES OF DELIBERATION</u>
<u>of the</u>
<u>ISLAND OF GUERNSEY</u>

POLICY & RESOURCES COMMITTEE

FUNDING AND INVESTMENT PLAN UPDATE

The Presiding Officer
States of Guernsey
Royal Court House
St Peter Port

11th September 2023

Dear Sir

1. Executive Summary

1.1 This policy letter sets out the results of detailed analysis undertaken by the Policy & Resources Committee since March 2023 following the debates on the Tax Review in January and February. The Committee initiated a range of projects to deliver on the States' resolutions following that debate (which are detailed in Annex 1), and many of those workstreams are ongoing.

1.2 At the same time, the Committee initiated the required review of the capital portfolio for this term. This was done as a matter of urgency as the Committee was concerned that a number of projects were awaiting funding decisions and it was no longer clear whether the portfolio was affordable. The review, along with the work to update the Funding & Investment Plan (F&I Plan), quickly showed that the baseline position was precarious, unaffordable and required urgent action. Without such action it became clear that the States would run out of reserves by 2029 and would then have no means of affording further investment in capital, not even routine or 'minor' capital.

1.3 Given this position, the Committee decided to extend the financial modelling over a ten-year period to focus not only on the financial position for this States but the underlying legacy position to be inherited by future States.

1.4 The F&I Plan covers all aspects of general revenue income and expenditure and social security income and expenditure, plus capital expenditure. It has been developed using best estimates based on informed assumptions and as such, it cannot be seen as a firm indication of what will happen over this period.

1.5 Although there have been changes since the F&I Plan was first published the key messaging remains the same. The following pertinent paragraphs from the original policy letter[1] published in 2021 convey a message which remains the same today:

"COVID-19 and Brexit have presented significant financial challenges in the recent past, but there are other pressures that have a more profound and lasting impact on our finances such as the implementation of NICE TAs in 2021, underlying health service cost pressures and other growing service demands due to an ageing population and increase in chronic illness. These other pressures are providing a real challenge in the short, medium and long-term, resulting in very little general revenue surplus to be invested in capital or other activity not covered by current committee budgets.

This is the time to deliberate on a different approach to public finances and consider borrowing money to invest in our island's future. The Policy & Resources Committee is setting out a recommendation that is affordable in the medium term to utilise existing financial assets and borrow a further £200m to invest in our infrastructure, improve our financial resilience and boost economic recovery and expansion. The Policy & Resources Committee does not make this proposal lightly, but the alternative is simply not in the best interest of our community. The Committee will seek to only borrow what is required to fund capital investment and would look for the most cost effective and low risk debt option to deliver on the ambition of the States and ensure financial security over the medium term.

This is a five-year medium-term plan, but the Policy & Resources Committee is acutely aware that the approach set out is not sustainable in the long-term. The proposal to borrow, in addition to the usual utilisation of reserves to support the capital requirements over the current term, is intended to enable the immediate progression of the States' priorities. However, this is a temporary solution only and a way of managing and not removing the underlying structural deficit. Without further action, beyond 2025 the States will again have to consider how best to support their spending requirements in the face of the same pressure to provide for the increased demand for existing services and maintain an appropriate level of capital investment. Reserves will have been depleted with only very limited surpluses being generated to top them up. A longer-term solution is required, and the provision of that solution will span the consideration of expenditure (covered within the States' priority 4 – reshaping government), economic growth (included within the recovery actions of the GWP) and raising additional revenues (with proposals from the Tax Review due to be considered by the States in September). All three elements will be required to achieve a sustainable solution within the principles of the Fiscal Policy Framework."

[1] Billet d'État No XV

1.6 What is clear is that the States cannot continue "as-is". Latest forecasts estimate that, without action, cash reserves available to fund general revenue and capital expenditure will be depleted in just over 5 years. The Assembly therefore must agree measures to improve the current financial position so that the States can continue to afford the critical services they provide to the island, invest for future generations and improve services in response to community needs.

1.7 The States must retain sufficient liquidity to remain financially stable. Cash reserves cannot be depleted to fund this term's capital portfolio leaving little or no reserves for next term. If cash reserves run too low the States will find they are in a position where there are insufficient funds to run key services or pay for critical infrastructure and they will not be in a strong enough financial position to secure new debt on favourable terms. A plan must be agreed now, by this Assembly, to ensure that this does not happen.

1.8 The latest refresh of the F&I Plan sets out a number of scenarios, including a way for the States to return to a position of long-term sustainable balance. All of these scenarios rely upon a core set of decisions which must be taken now in order to secure the short to medium term affordability position. These core elements require decisions in principle on limited new revenue raising initiatives and the delivery of cost saving measures.

1.9 Scenario 1 significantly reduces the available funds to this term's major capital portfolio to allow reserves to be maintained at tolerable levels in the medium term without any new borrowing being taken out. This scenario only delays the critical decision as to how the island can return to long-term balance to the next term, as well as accumulating infrastructure projects for future States. This scenario, while stabilising the short-term position, shifts responsibility to the next Assembly to agree how the States will achieve financial sustainability, and they will not be in a position where this decision could be delayed any further without serious consequences.

1.10 Scenario 2 builds on this by recommending that £200m of new borrowing is taken out. This borrowing allows sufficient cash reserves to be maintained in the short-term while increasing the level of funding available for this term's capital portfolio, deemed vital owing to previous underinvestment in public assets infrastructure.

1.11 Scenario 2 assumes the use of the Health Service Reserve to part fund the hospital modernisation programme capital expenditure. While this allows both the 'The Education Programme' and 'Our Hospital Modernisation Programme (OHM) Phase 2' to progress in full it does put further strain on remaining reserves. Currently the ongoing annual cost of NICE TAs[2] are funded through the Health Service Reserve, but in Scenario 2 these costs will be funded from general revenue from 2025 onwards as the full balance of the reserve will be committed to the OHM project. Although this scenario is affordable in the short-term and allows a greater amount of funding to be made available to progress key capital projects, the States must acknowledge it puts increased pressure on the next Assembly to agree a plan on how the island's finances can return to long term balance.

1.12 Scenario 3 builds on the other two scenarios by implementing the full progressive tax[3] package as previously considered by the States in early 2023. It recommends increasing new borrowing to a maximum of £350m, which is affordable because of the improved financial position. It allows for the capital portfolio to be funded in full as requested by all committees yet still retaining cash reserves at a healthy level. Critically it does not require the use of the Health Service Reserve to part-fund OHM Phase 2 project, providing additional flexibility and resource to manage demographics through service changes. This scenario allows for greater capital investment this term, which is deemed an important enabler for economic growth and resilience as well as ensuring health and education infrastructure investment requirements are met in full.

1.13 In addition, Scenario 3 enables £2.5m per annum to be ringfenced for new initiatives such as a green fund that could be used to provide insulation credits to encourage homeowners to make energy efficient homes and/or funding for arts or sports initiatives.

1.14 In summary the three scenarios presented to the Assembly in this policy letter are all affordable in the short to medium term, however, only Scenario 3 provides a sustainable pathway back to long-term permanent balance – the guiding principle of the States' own Fiscal Framework.

1.15 Scenarios 1 and 2 only put a 'sticking plaster' on the issue of financial balance, while further delaying the critical decision as to how the States will achieve a financially sustainable position.

1.16 However, even with the implementation of the measures in Scenario 3, there will be a need for further review over the coming years to ensure continued financial sustainability. The projections included in the 10-year financial model that support this F&I Plan are built on sound assumptions, but the further out the financial projections go the more uncertain they become.

[2] National Institute for Clinical Effectiveness (NICE) Technology Appraisal (TA) drugs and treatments. Policy letter "Review of the Funding of Drugs, Treatments and Devices, dated 5th November 2019" (Billet d'Etat I, 2020)

[3] Billet d'État III, 2023

1.17 The Policy & Resources Committee's mandate includes the duty to advise the States on their financial resources, fiscal policy and economic affairs and it is therefore only able to recommend a solution that meets the needs of the Island in the medium to long term, rather than a short-term fix that fails to address the underlying issue.

1.18 Although Scenario 2 is an improvement to continuing "as-is" and allows sufficient funds to enable progression of key capital projects, it does so by placing significant pressure on scarce reserves at a time when the States should be protecting their liquidity as a matter of priority. In light of the stark assessment of the financial position, the Committee does not feel that a decision on sustainability should be further delayed and left for a new States to address at the outset of the next term.

1.19 The Committee sets out in this policy letter and associated Annexes a detailed assessment of the financial position of the States both today and modelled to 2032. It also sets out the extent of the capital investment required in public infrastructure. When faced with all of this, the Committee believes it has no choice but to reintroduce the tax package previously rejected by the States. Inevitably some will question why a different package has not been compiled and presented, perhaps one that does not contain a Goods and Services Tax (GST). The answer to that is simple – over two years of investigation and detailed analysis showed that the package offered the best overall solution for the people of the Bailiwick to fund essential public services.

1.20 The tax package as re-presented in the F&I Plan assumes a significant amount of revenue raising via a progressive combination of a restructured contributions system that adds an allowance for all contributors; a remodelling of the personal income tax system to add a reduced 15% tax rate on income up to £30,000; a larger personal income tax allowance and an adjustment to pensions and benefits to counter the inflationary effects of a GST. It is designed to spread the burden of revenue raising between businesses and individuals, and to redistribute the burden of tax on individuals so that the majority of households below the median income level will, in fact, be better off.

1.21 Further to the above it should be noted that the previously proposed tax package assumed a 5% GST with minimal exceptions, but a 6% GST with the option to zero rate all food items is considered as an alternative. This is not expected materially to change the impact of the package on low-income households, the savings made on GST on food being largely subsumed by the higher rate applied to all other items, although it is expected to make administration significantly more complex.

1.22 It is for this reason that the Committee feels duty bound to once again ask the States to support a package of measures outlined in Scenario 3 that will deliver on the requirement to achieve long-term permanent balance and invest in urgently needed housing, education and health facilities. The Committee did not plan or expect to be putting this matter back to the States for debate this term, but now feels there is no option but to do so. This Assembly must address the issues being faced and leave a sustainable legacy for the island, it's public services and the next Assembly.

2. Introduction

2.1 This second update of the F&I Plan is set against a backdrop of continued financial pressure owing to operating within a structural deficit. This policy letter summarises the more detailed analysis contained within the Funding & Investment Plan (Annex 1) and the Capital Portfolio Plan (Annex 2).

2.2 In the 12 months since the last F&I Plan update there have been some significant changes to the States' priorities. The States agreed[4] in the Tax Review debate at the beginning of 2023 that the longer-term financial position of the States of Guernsey is unsustainable, but the debate concluded with no agreement to take forward any of the proposed tax packages to address the growing structural deficit. However, the States did agree a series of workstreams to look at revenue raising measures including transport, corporate and visitor taxes, charges and levies. The States also agreed to develop cost saving measures and for a full review of the capital portfolio, both with the primary aim of reducing spend.

2.3 Originally the F&I Plan was designed as the financial planning framework for the current term of government and therefore spanned the five years from 2021 to 2025. The first update in 2022 focused on year-on-year change with the inclusion of 2021 actuals. In this update, in light of the recent tax debate and the current financial environment, there is a strong focus on financing and affordability, but most importantly it proposes a path to long term financial sustainability.

2.4 The timeframe for the F&I Plan has been extended to 2032 to be able appropriately to assess funding sources and affordability over the next ten years. This F&I Plan sets out measures that can be taken to bring Guernsey's finances back to a sustainable position in the longer term.

2.5 As stated in the original F&I Plan the aim is to provide a financial framework within which the States can operate. It does not replace the annual budgeting cycle through which firm budgets will be allocated or substitute the need for detailed investment appraisals to ascertain value for money and other investment benefits ahead of funding approvals.

[4] Resolutions, Billet d'État III, 2023

2.6 The guiding principle of the States Fiscal Policy Framework is a policy of a long-term sustainable position of permanent balance. This would mean generating an ongoing revenue surplus that is sufficient to afford necessary capital and transformation projects, as well as funding public services, covering the expenditure of the agreed strategic policies of government and ensuring reserves are maintained at an appropriate level. In the short term it requires the States to have sufficient liquidity to ensure that the priorities of government can continue.

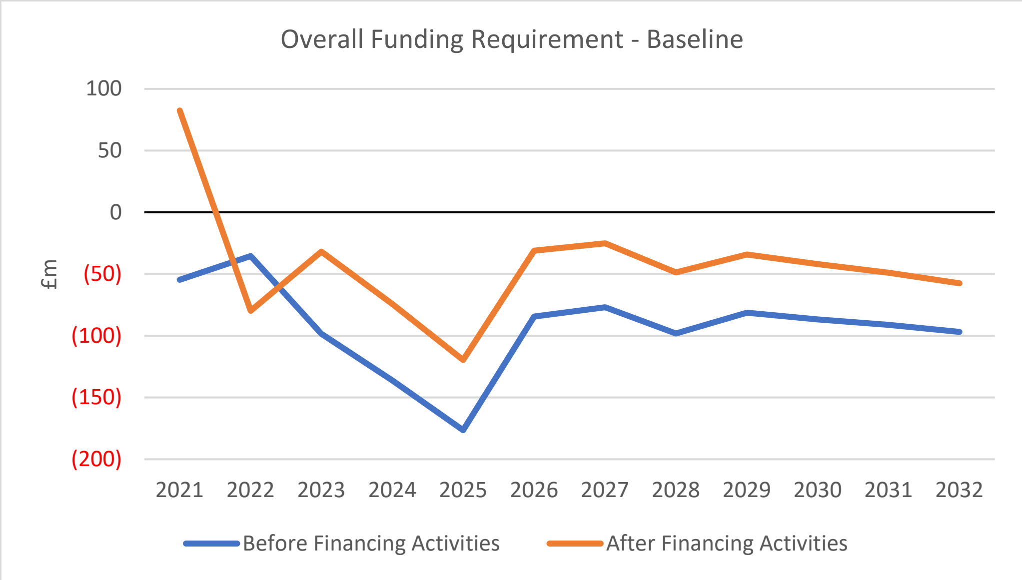
2.7 With regards to the States overall expenditure the following table indicates spend per capita for key government services, benchmarked against the UK and Jersey. As the table illustrates, overall Guernsey spends significantly less per capita than the UK and Jersey. If Guernsey spent £13,100 per capita like Jersey, then its cost base would increase by over £50m per annum. This data suggests that the States cost base is not unreasonable when benchmarked against other jurisdictions.

Spend per Capita £	Guernsey (incl Alderney, 2022)	Jersey (2022)	UK (2022-2023)
Population	65,747	103,267	67,220,000
Health, Social and Long-term Care	3,600	3,700	3,100
Pensions and benefits	3,800	3,500	4,800
Education	1,200	1,900	1,600
Other costs*	3,700	4,000	4,100
Total Cost per Capita**	**12,300**	**13,100**	**13,600**

**Including centralised services such as HR and IT*
***excluding financing charges, defence cost, and non-cash costs*

2.8 The chart below highlights the projected overall funding requirement from general revenue and social security income and expenditure. It includes capital expenditure rather than depreciation as this is the level of funding required in order to deliver infrastructure projects. The calculations have excluded any annual surplus or deficit of the Public Servants Pension Fund, the Seized Asset Fund or the Core Investment Reserve as these reserves are not available to fund services or capital expenditure.

2.9 The overall funding requirement is calculated as the general revenue income and social security contributions less associated general revenue and social security expenditure and capital expenditure. The chart highlights that spend is in excess of income which is driving the deficit (funding requirement shortfall).



2.10 The main difference between the two lines shown in the chart is owing to the investment returns, or losses, on the Guernsey Insurance Fund (GIF), the Long-Term Care Fund (LTCF) and the General Revenue Reserve (GRR). At the start of 2023 the GIF had a balance of £720m; the LTCF had a balance of £129m; and the GRR had a balance of £508m (including £160m of the existing unused bond proceeds) - these balances can therefore generate significant investment returns or losses.

2.11 For financial modelling purposes investment returns have been assumed at 2.5% above inflation equating to an approximate £35m return in 2023 for the GIF, £7m for the LTCF and £25m for the GRR. This is an appropriate long-term assumption as fluctuations to investment returns even out owing to the balanced portfolio of assets. However, year on year returns can vary significantly as was seen with the large returns made in 2021 compared to the significant losses in 2022.

2.12 Although the overall deficit has been shown including both general revenue and social security income and expenditure, the remainder of this policy letter will largely focus on general revenue income, expenditure, capital investment and reserves. The social security funds are ringfenced to support social security schemes and decisions have already been made to increase social security contributions over a 10-year period putting them onto a sustainable footing.

2.13 Capital investment is the focus of the F&I Plan rather than depreciation as it is key to understand cashflow requirements to ensure the States have sufficient liquidity to afford to progress their priorities. Section 4.11 to 4.16 of Annex 1 explains this in more detail.

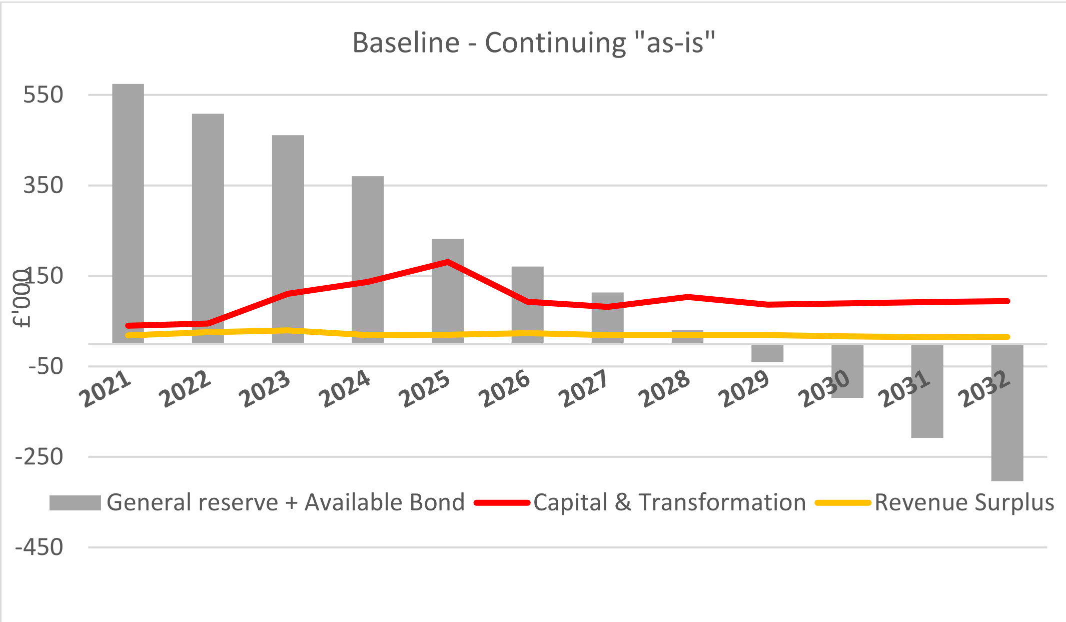
3. Baseline – Continuing “As Is”

3.1 The baseline presented in the F&I Plan is for comparative purposes only. It is not a valid option and the States have already resolved that it is not feasible to continue on the current trajectory.

3.2 The baseline model shows the projected financial position of continuing “as is” and assumes all actions previously prioritised within the GWP progress as planned, albeit at the most up-to-date cost estimates. It shows the financial impact of taking no further action with regard to cost cutting or revenue raising initiatives over and above what was agreed in the 2023 Budget.

3.3 The baseline model assumes that the States deliver the current capital portfolio as prioritised at the start of this term, although it has been updated to reflect latest cost estimates for all planned projects and programmes.

3.4 The following chart shows the impact of continuing “as-is” on the financial position.



3.5 The red line in the chart indicates the States’ planned investment in capital (major and minor) and transformation expenditure for this term’s portfolio and assumes that the current prioritised portfolio is delivered in full. From 2026 onwards, it is assumed that the equivalent of 2% of GDP per annum is invested in capital expenditure (in line with the current Fiscal Policy Framework assumption for major and minor capital).

3.6 The yellow line in the chart is the estimated revenue surplus (excluding social security income and expenditure). This is the surplus generated after all general revenue operating activities, but before financing activities such as investment returns and debt interest. Baseline surpluses are estimated to be minimal and would be extremely sensitive to investment returns and losses over the next few years.

3.7 For the States to be in a sustainable financial position, general revenue surpluses need to be generated at the same level as, or in excess of, the required capital expenditure. However, in the baseline the prioritised capital expenditure significantly outstrips any surplus generated resulting in the need to use cash reserves to fund the capital portfolio.

3.8 The grey bar in the chart shows the balance of the available reserves. The chart demonstrates that these will diminish quickly if relied upon to fund the capital portfolio and will run out by the beginning of 2029. That is just over five years away, during the next political term.

3.9 At this point the States would need to borrow to be able to fund future capital expenditure, illustrated by the negative grey bars. However, given the minimal general revenue surpluses, it would not be possible to afford the repayment of the principal amount. Any new debt that could be afforded at that point would also be on less favourable terms due to the precariously low cash reserves and there would be the very real risk of further credit rating downgrades.

3.10 Therefore, the Policy & Resources Committee has sought to put together a range of options that would address, in full or in part, the growing deficit and improve the States' financial sustainability.

4. Financial Position and Liquidity

4.1 Unlike the UK, the States of Guernsey are not a monetary authority. There is no central bank through which they can control monetary policy. A nation with this ability, such as the UK with the Bank of England or the USA with the Federal Reserve, can influence economic activity by manipulating the supply of money and credit and changing interest rates.

4.2 Guernsey is unable to do this, and it is therefore critical that the States manage island finances in a way that is sustainable.

4.3 In January 2023 Standard and Poor's Global Ratings (S&P) downgraded Guernsey's sovereign credit rating based on "*Guernsey's fiscal deficits and drawdowns from its financial assets*" further noting "*At the same time, global market turmoil has eroded Guernsey's significant asset buffer, which we estimate fell to 85% of GDP at the end of 2022".*

4.4 The report produced by S&P spanned four years from 2022 to 2026 and expected that Guernsey would likely push ahead with its significant capital spending programme despite forecast elevated deficits over this period. A key driver for the downgrade from an AA- rating to A+ was the significant erosion of cash reserves, estimating that assets had fallen to 85% of GDP in 2022 from a previous asset buffer of over 100%. Further, S&P projections assumed that liquid assets would reduce from 53.4% of GDP in 2022 to 45.9% of GDP in 2026 (an approximate £88m drop in liquid assets across the 4 years).

4.5 S&P acknowledged in the 2023 mid-year update that the outlook for Guernsey's A+/A- rating was stable; however, it went on to say:

"We could lower the rating if Guernsey's general government assets eroded by significantly more than we expect. This could happen if the consolidation measures implemented by the government prove insufficient to stabilize its funding needs."

4.6 It was further reported that:

"Increasing pressure on health and care services is intensifying the squeeze on public finances, while the shrinking working age population also threatens tax collections".

4.7 In short, the States cannot continue to spend more money than they bring in and they need to have a plan to return to a financially sustainable position in the medium term.

4.8 However, in the short-term liquidity must be maintained, not only from a credit ratings perspective, but most importantly for the States' own financial stability. Should the credit rating be downgraded any further, taking out new debt would become more expensive, be on less favourable terms, and the States could find themselves in a position of being unable to afford essential projects or to run key services.

4.9 Up until 2023, previous ratings downgrades suffered by the States have generally been triggered either by technical changes in the evaluation criteria, or external factors (such as the UK's exit from the European Union) and have applied equally to competitor jurisdictions. The latest downgrade was the first purely on the basis of a worsening in the States' financial stability and has led to a differential with other similar jurisdictions. The Committee strongly believes that it is important to stabilise this position and not suffer a further downgrade, which would widen the gap between Guernsey and its neighbours/competitors.

4.10 Currently the States have a debt-to-GDP ratio of approximately 9.5%, which is considerably less than other similar jurisdictions. For instance, Jersey, which has a credit rating of AA- (one notch above Guernsey), has an estimated debt/GDP ratio of 15.9% and is expected to grow to more than 22% based on current known plans. Bermuda, which has the same credit rating as Guernsey, has an estimated debt-to-GDP ratio of 41.5% and Malta which is one notch below at A- has around 58.5% debt-to-GDP ratio. This suggests that Guernsey has comfortable headroom to incur further debt from a credit rating perspective.

4.11 The Committee has been advised, and recommends to the States, that it is therefore essential that the States protect their cash reserves. To date the States of Guernsey have operated a "save to spend" approach whereby investment in capital is funded through historical surpluses. With depleting reserves and significant capital expenditure planned because of past under investment, this is no longer a sustainable position. The States need to ensure that there are adequate cash reserves to be able to invest in the future needs of the Island.

4.12 The scenarios set out in the F&I Plan are therefore based not only on meeting current requirements but with equal weighting on the importance of ensuring adequate liquidity and sufficient reserves are maintained for the next term's investment needs.

4.13 Further, assessments of Guernsey's financial health and resilience would generally consider reserves as a percentage of GDP. This includes the credit assessments by rating agencies which determine how much and at what rate the States might be able to borrow. Importance is therefore placed on maintaining reserves at their current percentage of GDP.

5. The Scenarios

5.1 Acknowledging that continuing 'as-is' is not an option the F&I Plan sets out three scenarios for consideration. Each of the scenarios presented has the same core elements, which include:

- Income measures – limited additional revenues including the implementation of pillar 2 corporate tax measures[5] and other corporate tax initiatives, an annual charge on vehicle ownership and other transport related taxes and visitor taxes. The total revenues forecast to be generated are estimated at £25m per annum.

- Expenditure savings - £10m of recurring annual savings implemented incrementally over 5 years.

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[5] OECD's Pillar 2 framework that introduces a global minimum corporate tax rate set at 15% to apply to multinational enterprises with revenue above EUR 750 million.

- Investing in policy development – covers the prioritised GWP policy initiatives plus assumes an additional £3m made available each year for future policy development.

- Core 'in-flight' capital projects – these schemes have already had substantive investment, are being delivered or are near completion and funding is therefore committed. There are 17 projects in this category that require funding of £96m in total.

5.2 In addition to the core elements listed above the funds allocated to the capital portfolio in Scenario 1 have been significantly reduced to ensure this scenario remains affordable in the short to medium term and cash reserves are protected. The funds available for this term's capital portfolio (excluding minor and transformation) from 1 January 2023 onwards are capped at £190m, with the next and future terms total capital expenditure (including minor capital and transformation expenditure) assumed to average 2% of GDP per annum. The £190m available for the capital portfolio would provide £94m for prioritised projects once funding is allocated to those 'in-flight' core projects that must be progressed.

5.3 Scenario 2 includes new borrowings of £200m to increase the funds available to this term's capital portfolio to be capped at £440m (from 1 January 2023 onwards), with capital expenditure assumed at 2% of GDP from 2026 onwards. The £440m available for the capital portfolio would provide £344m for prioritised projects once funding is allocated to those 'in-flight' core projects that must be progressed.

5.4 In this scenario, it is still only possible to progress both 'The Education Programme' and 'Our Hospital Modernisation Phase 2' if the Health Service Reserve is used to part fund the hospital project or new borrowing is taken out in excess of what is being recommended. For modelling purposes, the Health Service Reserve is assumed to be fully committed to the OHM Phase 2 project, meaning the NICE TAs, which are currently funded through this reserve, will need to be funded through general revenue from 2025. This will result in a further £5m per annum increase to the ongoing deficit. This scenario is only affordable in the short to medium-term and puts significant pressure on reserves with the full drawdown of the Health Service Reserve.

5.5 Scenario 3 assumes the implementation of the full progressive tax and benefits package[6] as proposed to the States in early 2023. New borrowings of £350m would further raise the funds available to this term's capital portfolio to £520m, with capital expenditure assumed at 2% of GDP from 2026 onwards. The £520m available for the capital portfolio would provide £424m for prioritised projects once funding is allocated to those 'in-flight' core projects that must be progressed. Additional borrowings would still be required to ensure reserves remained at adequate levels during the implementation phase of the tax package.

5.6 The full description and modelling assumptions of each scenario can be found in Appendix 2 and in the F&I Plan in Annex 1. Further details on corporate tax initiatives can be found in section 11 (paragraphs 11.29 to 11.42) of Annex 1.

5.7 In addition, section 12 of this policy letter, considers the effect of changes to key variables and assumptions on the financial projections. This is particularly important given the exceptional volatility in public finances seen over the last few years. Further detailed sensitivity analysis can be found in section 16 of the F&I Plan Report in Annex 1, which highlights the range of outcomes that could be expected including best- and worst-case scenarios.

6. Scenario 1

6.1 In summary, this scenario assumes that an additional £25m of annual revenues are generated through pillar 2 and other corporate tax measures as well as from an annual charge on vehicle ownership and other transport related taxes and charges. Cost savings have been assumed to increase from £2.5m per annum in 2024 to £10m per annum in 2029 in real terms. It is assumed that there are no new borrowings in this scenario.

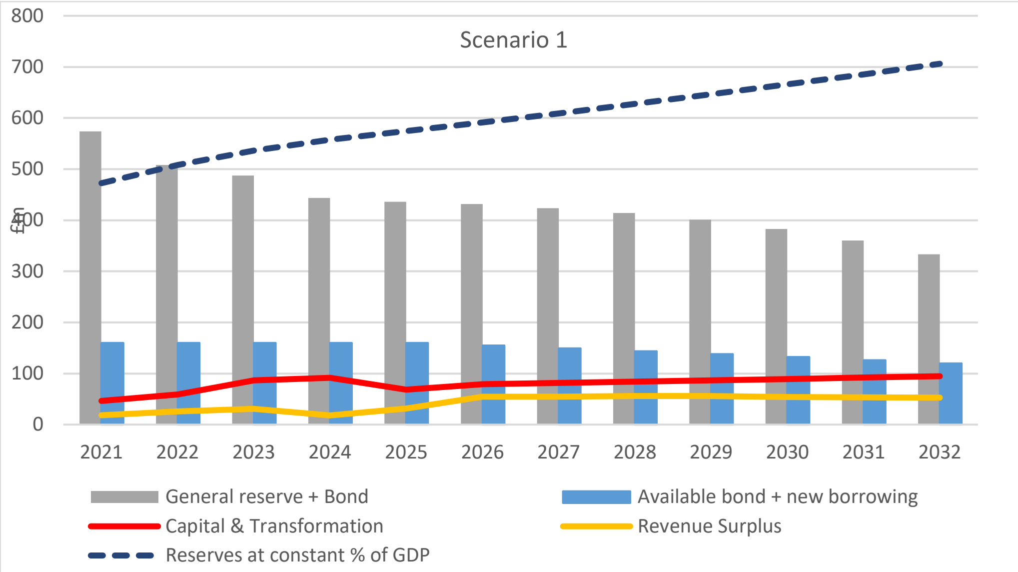
6.2 Full assumptions of Scenario 1, including the associated major capital portfolio assumptions, can be found in Appendix 2. Full details of the Scenario 1 capital portfolio can be found in Appendix 5.

6.3 Scenario 1 significantly reduces the funds available to the capital portfolio so that cash reserves are not depleted in the short to medium term without a plan as to how they will be replenished. However, the reduced funds available for capital expenditure still equate to approximately 2% of GDP for this term.

[6] Billet d'État III, 2023

6.4 The following chart summarises the projected financial position of this scenario. As per the previous baseline chart the red line highlights the projected capital and transformation spend, the yellow line shows the estimated revenue surplus before financing activities and the grey bars indicate the balance of the general revenue reserve (that is the reserves available for capital expenditure and funding government services).

6.5 This chart also illustrates by way of the dotted line what the reserves balance would be if maintained at a constant percentage of GDP based on 2022 closing reserves balance and the 2022 estimated GDP.



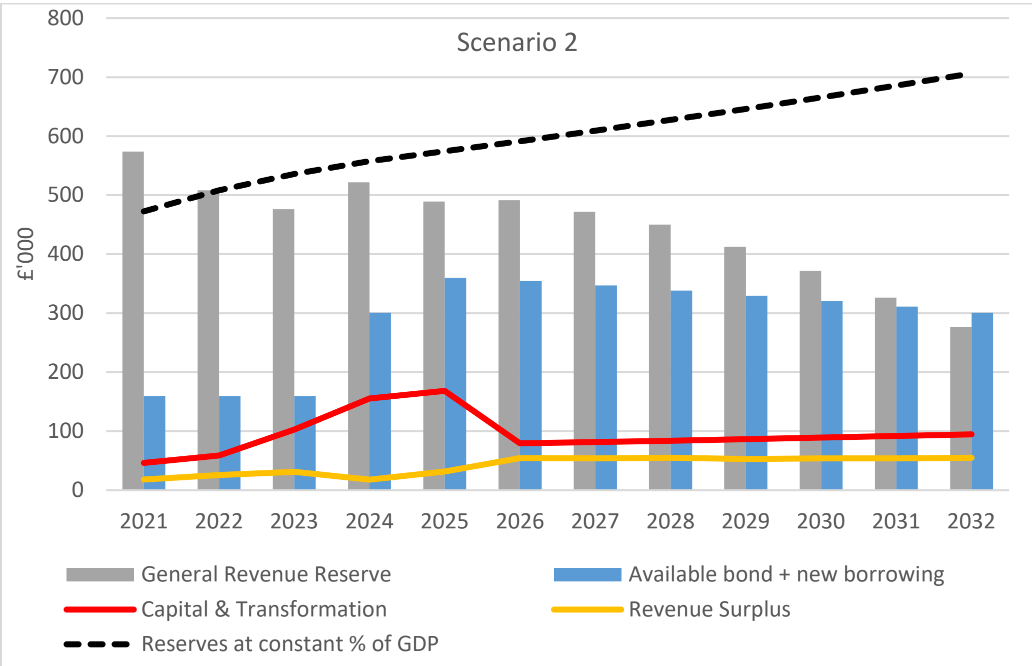
6.6 Although the financial position of this scenario is a marked improvement on the baseline, and it is affordable in the medium term, it does not bring the States back into a financially sustainable position. The revenue surpluses have increased, and the capital spend this term has been restrained, but not to the point where annual capital expenditure can be afforded from general revenue surpluses alone. It should be noted that the yellow line representing the annual surplus excludes investment returns, however, investment returns are included in the projected balance of the reserves (grey bars).

6.7 Reserves will still be required to part-fund the capital portfolio meaning that it would not be possible to sustain adequate reserves and liquidity in the longer term. The worsening of the financial position is further illustrated by the widening of the gap between the projected reserves if maintained at a constant percentage of GDP based on 2022 figures (dotted line) and the projected reserves balance based on this scenario's assumptions (grey bars).

7. Scenario 2

7.1 This scenario has the same modelling assumptions as Scenario 1 but includes new borrowings of £200m enabling more funds to be made available to the capital portfolio this term, while retaining sufficient levels of cash reserves for next term.

7.2 In addition to borrowing, it assumes the Health Service Reserve is used to part fund the 'Our Hospital Modernisation Programme Phase 2'. The NICE TAs will continue to be funded through the Health Service Reserve until the end of 2024, but after this date these costs will be funded through general revenue. Full details of Scenario 2, including the associated major capital portfolio, can be found in Appendices 2 and 5 respectively.



7.3 The red line on the above chart highlights the increased investment in capital expenditure during this term. The chart also shows the £200m of new borrowings taken out (blue bars) to ensure appropriate liquidity levels (grey bars) are maintained in the short and medium-term.

7.4 Once again, this scenario does not bring the States back to a sustainable financial position as reserves are being depleted at a significant rate owing to capital expenditure (red line) exceeding revenue surpluses (yellow line) on an ongoing basis, which is worsened through the additional cost of the NICE TAs. Crucially, under this scenario, sustaining adequate reserves would not be possible beyond the next political term.

7.5 This is further illustrated by the widening of the gap between the projected reserves if maintained at a constant percentage of GDP based on 2022 figures (dotted line) and the projected reserves balance based on this scenario assumptions (grey bars).

7.6 This scenario is affordable in the short to medium term, but the next Assembly would need to address the ongoing deficit as a matter of priority before cash reserves run precariously low.

8. Scenario 3

8.1 Scenario 3 not only incorporates the revenue raising and cost saving initiatives assumed in the other two scenarios, but also adds in the revenue raising measures (updated for inflation and social security contribution rate changes) proposed in the Tax Review policy letter debated in February 2023. With additional revenue raising, a higher level of capital investment can be made in the short to medium term and reserves maintained at a sustainable level with the introduction of £350m of new borrowing.

8.2 In addition to the increase in funding made available to the capital portfolio this scenario allows for £2.5m per annum to be ringfenced for new initiatives that result in a social or community benefit such as a green fund that could be used to provide insulation credits to encourage homeowners to make energy efficient homes and/or funding for arts or sports initiatives.

8.3 Full details of Scenario 3, including the associated major capital portfolio, can be found in Appendix 2 and Appendix 5.

8.4 The new revenue measures assumed in this scenario include the progressive tax package presented to the States in early 2023, which proposed a reduction in income tax and social security contributions for most lower- and middle-income households. This included the introduction of a personal allowance for social security contributions, an increase in the personal income tax allowance and the introduction of a 15% tax band on income between the personal tax allowance and £30,000. At the core of this restructure was a broad-based GST at 5%. The original tax package is being re-presented, rather than an alternative, as it remains the best solution for Guernsey based on a significant amount of work previously undertaken to consider different options to return to a sustainable financial position and taking into account the impact on households. The full details of the package proposed can be found in 'The Tax Review: Phase 2' policy letter[7].

8.5 This package is estimated to raise a net £59m, adjusted for inflation and earnings growth.

8.6 Of this, £26m would be raised from corporate entities via increases in employer contributions and an International Services Entities Fee within the GST structure that captures a larger contribution from the finance sector. A total of £26m will be raised from households with more than 60% of this coming from the richest 25% of households. This will mean most lower income households will be better off than under the current tax system, even after considering the additional costs incurred because of the GST. £7m is expected to be generated from visitor spend under this model.

8.7 This scenario, including the additional revenue raised from corporate and transport taxes, would raise aggregate government revenues from around 21% of GDP to between 23% and 24% of GDP. This would place Guernsey on a more comparable footing with Jersey, which raises around 26% of GDP in revenues, and would be within the principles of the States' Fiscal Policy Framework.

8.8 It would also broaden the tax base away from its current high concentration on taxes on income, providing greater resilience given the ageing demographic. Reviewing the experience in Jersey over the last decade, revenues from GST have typically moved quite differently to personal income tax revenues, with a weak year in one often coinciding with stronger growth in the other. Overall, the annual growth rate in GST over the last decade has averaged slightly higher than the growth in personal income tax receipts, which is reflected in this F&I Plan.

8.9 As part of the Tax Review debate there was much discussion about the application of GST to food. The Committee's preference would still be to apply GST on as broad a base as possible, as critically it makes the administration of the GST simpler and less expensive to run – important not only for businesses but also for the States.

[7] Billet d'État III,2023

8.10 For businesses, it means they have only a single rate to deal with and will not have to apply different treatments to different product lines. It is also likely to reduce compliance activity for businesses. For the Revenue Service, it reduces the likelihood of error in the submission of quarterly returns and minimises compliance activity. For the Guernsey Border Agency, it reduces the complexity involved in determining whether imported goods are taxable, or, if they face a mixed delivery, how much of the value of the import is taxable and how much zero rated.

8.11 It is for these reasons that many jurisdictions including Jersey (2009), New Zealand (1986), Saudi Arabia (2018) and UAE (2018) have introduced broad-based and relatively low-rate schemes with only limited exemptions or zero-rating. All of these systems include a GST or similar tax on food.

8.12 If a zero rate were to be applied to food, it would reduce the revenue generated and make it necessary to apply a higher rate of 6% to all other taxable goods and services in order to raise the same amount of revenue. In doing so almost all the benefit to lower income households is lost.

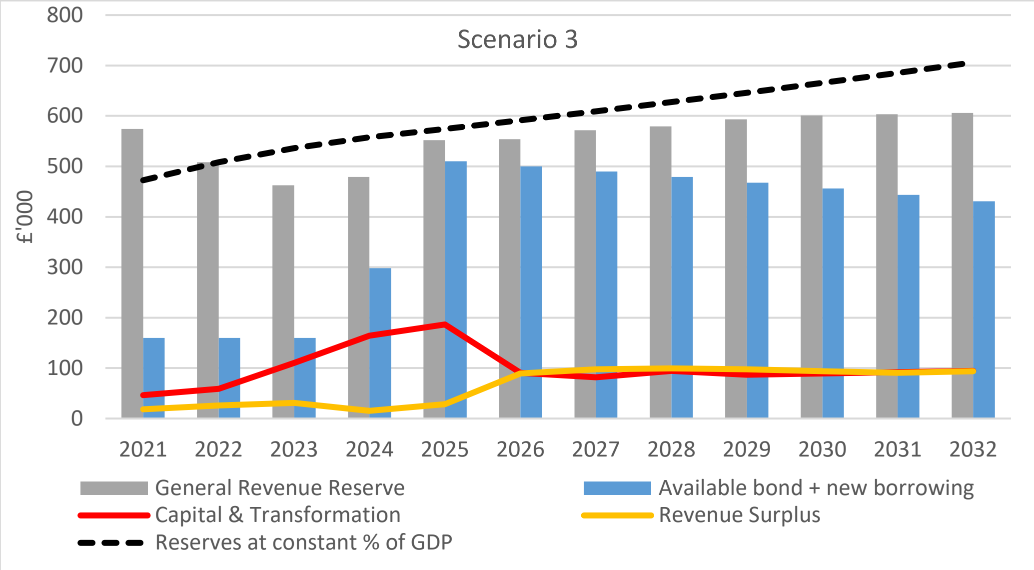
8.13 While analysis shows that lower income households spend a higher proportion of their income on food than higher income households, in monetary terms higher income households spend significantly more. This means that the benefit of zero-rating food is poorly targeted and in monetary terms more of the lost revenue is to the benefit of households in the richest 30%.

8.14 It is recommended that a full review of GST takes place by 2032 (the end of the timeframe this F&I Plan considers) to ensure rates are set at applicable levels and to confirm that such tax is still required. It is proposed that legislation required to introduce GST has both a commencement date and an end date. This will ensure a review is undertaken in a timely manner.

8.15 In Scenario 3, with the introduction of the full tax and benefits package, the States shift into financial stability illustrated in the chart below by the convergence of the red and yellow lines.

8.16 New borrowings of £350m are proposed to ensure appropriate liquidity is maintained in the short term as the phased measures of the progressive tax and benefits package are rolled out. This enables a higher investment to be committed to this term's capital portfolio.

8.17 This level of borrowing is affordable in Scenario 3, with repayment and interest on the debt included within the financial modelling. The repayment and interest expense are included in the reserves and debt balance on the following chart.



8.18 The chart illustrates that annual surpluses are sufficient to cover expenditure. However, even under this scenario, although reserves can be rebuilt to some extent, their value relative to GDP is projected to fall from current levels.

9. Capital Prioritisation in the Scenarios

9.1 As referenced in the 2021 Funding & Investment Plan a review of the capital portfolio was planned to take place during the term as the portfolio of projects matured.

9.2 Further to this a Resolution of the Tax Review debate directed the Policy & Resources Committee to engage with Principal Committees and wider States' Members to review the capital portfolio and pipeline in light of the outcome of the debate and to report back to the States by March 2024.

9.3 While the direction was for the review to be completed by March 2024, the Committee decided to accelerate the review of the existing capital portfolio and its funding given the number of projects that were due to come forward for funding post the tax review debate.

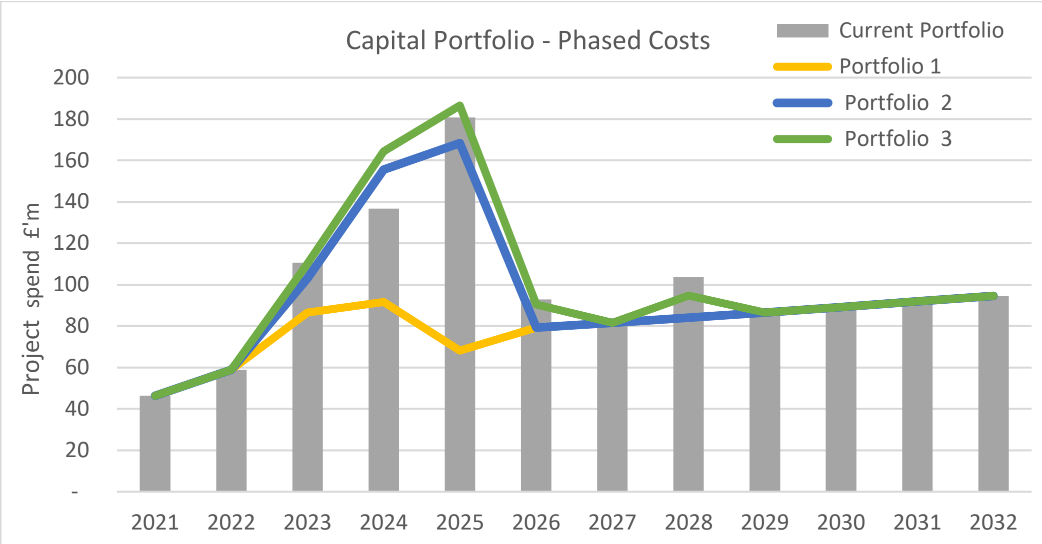
9.4 The resulting capital portfolio options that are proposed within this F&I Plan update are therefore based on this review and the affordability of each scenario. Further details of the capital review and the proposed options can be found in the 'Capital Portfolio Report' in Annex 2.

9.5 From an affordability perspective each of the three scenarios enables a different amount of funding to be made available for the remainder of this term's major capital portfolio:

i. Scenario 1 - £190m
ii. Scenario 2 - £440m
iii. Scenario 3 - £520m

9.6 It should be noted that the value of these portfolios is calculated on the funding required to complete the schemes noting that many will already have incurred cost to date.

9.7 The chart below illustrates the forecast phased spend of each of the portfolio scenarios:



9.8 Deliverability, in addition to affordability, was a significant consideration in the review of the capital portfolio. Scenarios 2 and 3 both pose scheduling challenges owing to several large and complex projects being delivered at similar times. Work is ongoing to ensure a plan is in place to deliver the projects prioritised within each of the scenarios within the limited resources available.

9.9 There are a number of projects that are already underway with funding approved and contractual obligations in place. These projects will require £96m in total to complete and are included in all three scenario portfolios. These schemes are categorised as 'In flight' and include:

1. Our Hospital Modernisation (OHM) Phase 1
2. Electronic Patient Record
3. Digital Infrastructure
4. Funding Affordable Housing Developments Programme
5. IT Transformation
6. Revenue Service Programme
7. VME Replacement
8. Guernsey Registry IT Systems Replacement

9. Online Passport & Workflow System
10. Footes Lane Refurbishment (near completion)
11. Sarnia Cherie BWMS (near completion)
12. Mont Crevelt Breakwater Reinstatement
13. Transforming Education Digital (secondary and primary)
14. SMART Court Phase 1
15. MyGOV Programme (near completion)
16. Havelet Slipway Repairs
17. Tetra PSN

9.10 A summary of each of the proposed portfolios and the projects prioritised within them are set out in the table below (and in more detail in Annex 2):

Do As Planned		
Portfolio 1	**Portfolio 2**	**Portfolio 3**
Property Rationalisation Phase 2	Property Rationalisation Phase 2	Property Rationalisation Phase 2
Clinical & Animal Waste Solution	Clinical & Animal Waste Solution	Clinical & Animal Waste Solution
Community Services (Children & Families Hub)	Community Services (Children & Families Hub)	Community Services (Children & Families Hub)
Supply Chain Relocation (Central Stores)	Supply Chain Relocation (Central Stores)	Supply Chain Relocation (Central Stores)
Bridge Regeneration (Housing & Flood Defence)	Bridge Regeneration (Housing & Flood Defence)	Bridge Regeneration (Housing & Flood Defence)
Future Harbour Requirements - Survey	Future Harbour Requirements - Survey	Future Harbour Requirements – Survey
Alderney Airport Pavements Rehabilitation	Alderney Airport Pavements Rehabilitation	Alderney Airport Pavements Rehabilitation
Repair/Replacement of Castle Emplacement Bridge	Repair/Replacement of Castle Emplacement Bridge	Repair/Replacement of Castle Emplacement Bridge
	Our Hospital Modernisation (OHM) Phase 2	Our Hospital Modernisation (OHM) Phase 2
	Transforming Education Programme	Transforming Education Programme
		Future Inert Waste Facility
		SAP Roadmap

Do But Review Scope &/or Solution		
Portfolio 1	**Portfolio 2**	**Portfolio 3**
Guernsey Airport Pavements Rehabilitation (PFOS)	Guernsey Airport Pavements Rehabilitation (PFOS)	Guernsey Airport Pavements Rehabilitation (PFOS)
Fermain Wall	Fermain Wall	Fermain Wall
	Bus Fleet Replacement Phase 3	Bus Fleet Replacement Phase 3
	SMART Court Phases 2 & 3	SMART Court Phases 2 & 3

Pipeline		
Portfolio 1	**Portfolio 2**	**Portfolio 3**
CCTV Replacement	CCTV Replacement	CCTV Replacement
Coastal Flood Defences	Coastal Flood Defences	Coastal Flood Defences
Guernsey Airport Runway Infrastructure	Guernsey Airport Runway Infrastructure	Guernsey Airport Runway Infrastructure
Home Affairs Estate Rationalisation	Home Affairs Estate Rationalisation	Home Affairs Estate Rationalisation
Community Hub (HSC)	Community Hub (HSC)	Community Hub (HSC)
HSC Digital Roadmap	HSC Digital Roadmap	HSC Digital Roadmap
Future Guernsey Dairy	Future Guernsey Dairy	Future Guernsey Dairy
Future Harbour Requirements	Future Harbour Requirements	Future Harbour Requirements
Our Hospital Modernisation Pathology	Our Hospital Modernisation Pathology	Our Hospital Modernisation Pathology
Future Inert Waste Facility	Future Inert Waste Facility	
SAP Roadmap	SAP Roadmap	
Our Hospital Modernisation Phase (OHM) 2		
Transforming Education Programme		
SMART Court Phases 2 & 3		
Replacement Phase 3		

9.11 Each of the portfolios includes an allocation of £35m for the Bridge Regeneration project which is aimed at providing key worker housing. This is considered essential to easing operational pressures across the public sector workforce. This scheme also includes accelerating the St Sampson Harbour bridge flood defence work, part of the much broader Coastal Flood Defences scheme which is in the pipeline.

9.12 The funding agreed for the feasibility study in respect of the Future Harbours programme has also been included in each portfolio recognising the States' recent resolution following consideration of the East Coast Development policy letter[8].

9.13 Portfolio 1 has the least amount of funding available to it and therefore has a smaller number of prioritised projects. In addition to those core projects that are already 'in flight' it has a strong focus on delivering affordable housing as well as providing funding for those projects which are deemed 'must do'.

9.14 Portfolio 2 expands on Portfolio 1 and includes additional funding for education and health, amongst others. By utilising the Health Service Reserve for health-related capital expenditure and taking out £200m of new borrowing, the funding made available enables the progression of both "Transforming Education Programme" and "Our Hospital Modernisation (OHM) – Phase 2".

9.15 Portfolio 3 has the largest amount of funding available and would enable the States to build on Portfolio 2 so that both the health and education programmes to be delivered in full as currently planned. The portfolio would also provide funding for the Inert Waste Facility to project completion. This scenario does not use the Health Service Reserve for capital expenditure but does assume additional borrowing of £350m.

10. Funding

10.1 The following table provides a summary of the three scenarios and the available funding for the current term's capital expenditure in order to demonstrate the affordability of the differing capital portfolio options for this term only.

10.2 The capital funds required are shown in the lower section of the table and differ to the amounts referenced above because of the inclusion of minor capital and transformation, which are in addition to the major capital portfolio. Both the surpluses included in the 'available funding' section of the table and the capital funding requirement in the lower section are <u>for this term only</u>.

[8] Billet d'État XV, 2021

10.3 The surplus for Scenario 3 is £6m lower than Scenarios 1 and 2 due to £5m being ringfenced for social and community initiatives. A further £1m cost is because of the revenue impact of the increased capital portfolio.

Existing Reserves/Bond £m	Balance	Available to Use			
	31.12.22	Baseline	Scenario 1	Scenario 2	Scenario 3
General Revenue Reserve	348	-	-	-	-
Bond	160	160	160	160	160
Health Service Reserve	112	26	26	94	26
Revenue Surplus (2023-25)[1]	-	69	81	81	75
New Borrowing		-	-	200	350
Available Reserves	**620**	**255**	**267**	**535**	**611**

Capital Funds Required This Term[2]	**Total Capex**	**588**	**266**	**526**	**608**
	Baseline	588			
	Portfolio 1		266		
	Portfolio 2			526	
	Portfolio 3				608

1. *Excludes investment return*
2. *Includes major, minor & transformation*

10.4 The above table assumes that the current balance of the General Revenue Reserve is retained rather than drawn down to fund capital expenditure. This is to ensure the retention of sufficient cash reserves for next term and future years as argued in section 4 above.

10.5 The available balance of the existing bond proceeds (£160m) is allocated to part fund the capital portfolio as agreed in the 2021 Funding & Investment Plan.

10.6 The Health Service Reserve can only be used to fund expenditure if it meets specific criteria. In Scenarios 1 and 3 it is assumed the NICE TAs and the Committee *for* Health & Social Care's current initiatives to reduce waiting lists are funded from this reserve. By the end of the 10-year time frame the reserve is estimated to have a remaining balance of £47m in both these scenarios.

10.7 Scenario 2 assumes the Health Service Reserve is used to part fund OHM phase 2, the current waiting list initiatives and the NICE TAs through to the end of 2024. Therefore, in Scenario 2 this reserve will be depleted in 2024 and ongoing costs will be met from general revenue.

10.8 New borrowing is proposed at affordable levels in both Scenarios 2 and 3 to enable greater levels of funding to be released to the capital portfolio while maintaining cash reserves.

10.9 However, borrowing to fund prioritised services and projects that do not generate an income stream is a short-term solution only and although borrowing spreads the cost of assets, if all capex is funded through borrowing it will end up being more expensive due to the cost of financing. Furthermore, the States will need to ensure they plan for a future sustainable financial position to pay back any borrowing they may decide to take out, and importantly start to build up reserves once again to meet the future investment needs of the Island.

10.10 When considering borrowing and the best type of debt facility flexibility is important, especially when timing and value of cashflows are uncertain, to ensure new debt is only incurred when required to avoid unnecessary costs. It was determined the key factors to consider when assessing the use and type of debt to fund the capital portfolio includes:

i. Minimise Funding Costs: capital spend is forecast over a number of years, so it is important that new debt is entered into only when required. This will minimise costs, and risk, on unutilised debt funding over an extended period. Estimating the cashflow requirements of the capital portfolio has historically been challenging, which further increases the importance of the flexibility requirement.

ii. Funding Security: to reduce market risk exposure for future cashflows and to minimise risk that funding is not available on acceptable terms or pricing when required.

iii. Preserve or Improve Credit Rating: to ensure that an appropriate level of cash reserves is protected and that any debt facility will help minimise against further downgrades.

10.11 Given the difficulty in estimating accurately the timing of the projected cashflows of the capital portfolio and acknowledging that projections will change and become more accurate as projects mature and progress through the planning and implementation phases of the project lifecycle, a “bridge-to-bond” structure is recommended.

10.12 As the funding requirements of the capital portfolio are phased over a number of years it is not advised that a bond is taken out until the cashflows have been incurred or are highly likely to incur imminently, otherwise the States will be paying for a debt facility they are not using. This would not be cost effective. Timing of debt issuance is key to minimise costs while balancing the need of funding security.

10.13 A "bridge-to-bond" is effectively where a bank facility, such as a Revolving Credit Facility, is utilised to fund cashflows until the facility reaches a certain size. When appropriate and once debt reaches a certain level, the bank facility can be converted into a bond. This financing strategy is thought to meet the objectives of flexibility, while minimising funding costs and attaining funding security.

10.14 A public bond is considered the most cost-effective way of raising external debt and is available over longer tenures ranging from 10 to 50 years. However, the minimum issuance size is £250m for optimal execution and terms, though smaller issuances are possible but would attract an illiquidity premium.

10.15 For smaller issuances from £50m upwards a US or UK private placement could be considered. A private placement is similar to a public bond in terms of being a longer dated instrument, but it will likely have restrictions more similar to a bank facility. Should borrowing be required at £200m then a more detailed analysis of the risk and benefits of a public bond versus a private placement would need to first be undertaken.

10.16 In addition to the key funding objectives of cost, flexibility and funding security consideration should be given to environmental, social and governance (ESG) factors when determining the most suitable long-term debt financing facility. This could be in the form of 'green' bonds where the money raised targets environmentally friendly projects such as renewable energy, or perhaps a better suited 'social' bond where the focus is on projects with positive social outcomes, such as improving health or providing affordable housing. A social bond is also likely to come with better rates, linking into the key objective of minimising borrowing costs.

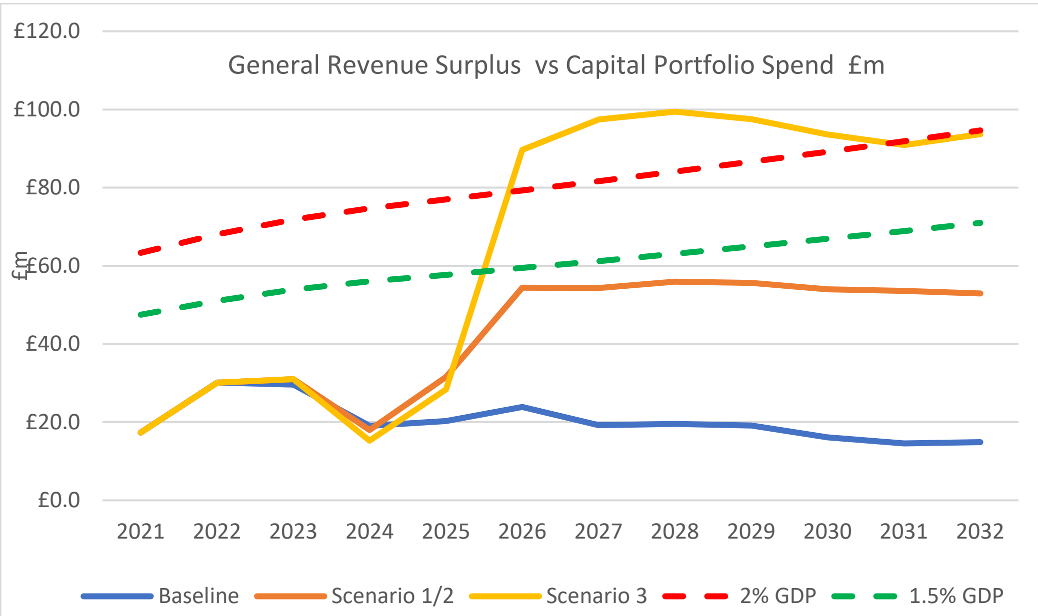
11. Summary of the Scenarios

11.1 The nominal (including inflation) changes in general revenue income and expenditure from the baseline projections to Scenarios 1, 2 and 3 are set out in the following table:

Revenue Surplus - £m *(Before Financing Activities)*	2024	2025	2026	2027	2028	2029	2030	2031	2032
Baseline	**19**	**20**	**24**	**19**	**20**	**19**	**16**	**15**	**15**
Corporate Tax	-	-	16	17	17	18	18	18	19
Annual Vehicle Charge	-	11	11	11	11	12	12	12	13
Savings	3	4	6	8	10	12	12	12	13
GWP Initiatives	(4)	(4)	(3)	(3)	(2)	(2)	(2)	(2)	(2)
RICE (option b)	-	-	1	2	-	(2)	(2)	(2)	(4)
Scenario 1 & 2	**18**	**31**	**55**	**54**	**56**	**57**	**54**	**53**	**54**
Full Tax Package Impact	-	-	39	49	47	45	43	40	42
RICE (option a)	-	(1)	(1)	(3)	-	-	-	-	2
Scenario 3	**18**	**30**	**93**	**100**	**103**	**102**	**97**	**93**	**98**

11.2 The table also highlights the estimated surpluses, before financing activities, with baseline surpluses estimated to reach as low as £15m by 2031, increasing to circa £55m for Scenarios 1 and 2 and increasing to circa £100m for Scenario 3.

11.3 To achieve a long term sustainable financial position and permanent balance, the States need to have a general revenue surplus higher than their capital expenditure requirements, regardless of how those requirements are financed. In the following chart the solid line (the revenue surplus) needs to be higher than, or equal to, the dotted line (capital expenditure) to be in a sustainable position.



11.4 The baseline shows an increasingly negative picture, with very small surpluses generated, nowhere near sufficient to cover the cost of investing in the current prioritised capital projects or be able to invest in future terms' capital requirements.

11.5 Scenarios 1 and 2 with the limited additional revenues and cost savings result in an improved position. However, the surpluses are not sufficient to cover capital expenditure requirements at 2% or even 1.5% of GDP and therefore do not provide a financially sustainable position and will still require further revenue raising to be agreed in the next term.

11.6 Scenario 3, which includes the progressive tax and benefits package, results in a significantly improved financial position bringing the States back to financial sustainability by 2026 i.e. early in the next political term.

12. Risks & Opportunities

12.1 There are a number of risks and opportunities associated with the scenarios and projections set out in the F&I Plan. These are explained more fully in the main body of the attached F&I Plan (Annex 1), but this section highlights the main risks and opportunities.

<u>Savings Realisation</u>:

12.2 Historically the States do not have a good track record of successfully delivering savings targets and there is a significant risk that the £10m real terms savings (£13m in 2032 in table in paragraph 11.1 because of inflation) built into the three scenarios will not be fully realised.

12.3 However, there is also a small upside opportunity if it proves possible to find the upper end of the cost reduction target of £16m.

<u>Baseline Cost Control:</u>

12.4 There is the risk that baseline costs increase above that provided for in the F&I Plan scenarios. Allowance has been made for any known increases to the cost base already agreed by the States as well as an estimate for future changes in demand which will lead to increased cost. However, there is risk that costs could increase in excess of this.

12.5 An example could be Health & Social Care where the ageing population is having a significant impact on service demand. A £4m per annum real-terms increase to the Health & Social Care baseline costs has been factored into the model based on analysis undertaken internally and as part of the hospital modernisation work, but there is a risk that demand pressures may lead to costs in excess of this.

New cost pressures, including Supported Living and Ageing Well Strategy (SLAWS):

12.6 The GWP includes a range of workstreams which may result in additional cost to the States once policy work is concluded and proposals for changes to service provision are brought back to the States. An example is the ongoing workstream prioritised within the GWP to address the long-term care model - SLAWS. The ongoing costs of the existing long term care scheme and the increased revenues previously agreed by the States to fund this have been factored into the projections on the LTCF. However, given the extant Resolutions driving this work seek to increase the range of services available to be funded through the scheme, it is possible that the proposals for a new model of care will emerge which increases the costs of the scheme in order to deal with pressure on the health and social care budget. It has been assumed that any such service change and cost increases will be accompanied by proposals for their funding. These are still being worked through and will return to the States by the end of Q2 2024.

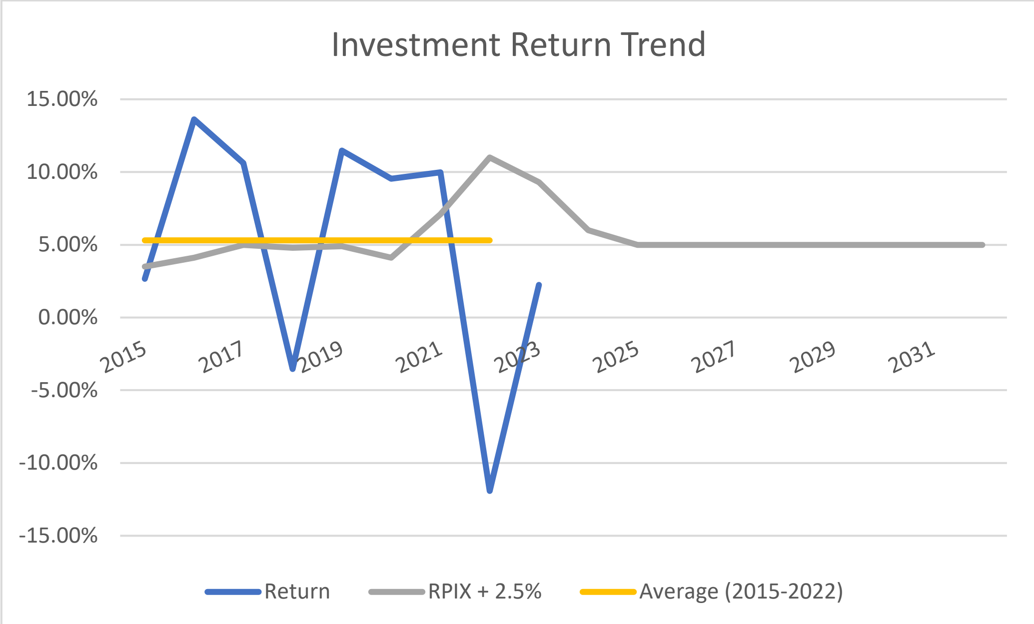
Income:

12.7 There is both risk and opportunity to the level of income projected in each scenario. States income depends on a wide variety of factors, such as economic conditions, inflation, and the state of the housing market and these can be difficult to predict with a high degree of certainty, particularly when forecasts extend over a ten-year horizon. This is further exacerbated in Guernsey because its small size means that some revenue streams, such as corporate tax receipts, can undergo significant shifts based on the decisions of a small number of larger companies. Forecasts should be seen as representing the most likely outcome on average over time under normal conditions, and it should be expected that individual years will differ from the forecast out turn.

12.8 Revenue streams such as document duty, corporate tax and investment returns are considered to have a high level of forecasting risk, whereas personal income taxes, social security contributions and excise duties are considered to have a moderate level of forecasting risk. TRP and rental income streams are considered a low forecasting risk.

Investment Returns:

12.9 Investment returns are highly volatile as seen over the last two years and illustrated in the following chart. The long-term average of 2.5% above inflation has been assumed but in reality, annual returns will be either higher or lower than this.



New Initiatives:

12.10 There is further risk and opportunity to the phasing in and implementation of any new measures, which may take longer than anticipated resulting in the delay of new income streams.

12.11 The following tables illustrate the potential impact of key risks and opportunities to general revenue income and expenditure. The estimated annual impact has been adjusted in line with the likelihood of the event occurring.

Income/Expenditure Risk 2024-32	Estimated impact on model (£m per annum)	Likelihood (%)	Net Risk (£m per annum)
Cost savings not realised	10	65%	7
Baseline cost overspend by 5%	29	20%	6
New initiatives/costs not planned	10	50%	5
Income 5% lower than forecast	30	20%	6
Investment returns 0% +RPIX	12	30%	4
Total	**91**		**28**

Income/Expenditure Opportunities 2024-32	Estimated impact on model (£m per annum)	Likelihood (%)	Net Risk (average £m per annum)
Cost savings fully realised (to £16m)	6	10%	1
Baseline cost underspend by 5%	29	10%	3
New income initiatives not planned	10	65%	7
Income 5% higher than forecast	30	40%	12
Investment returns 5% +RPIX	12	30%	4
Total	**87**		**27**

13. Conclusion

13.1 It is evident from the financial modelling and associated analysis that the only way back to a permanent long-term balance is through a combination of cost saving initiatives and significant income raising measures. Scenario 3 in this update of the F&I Plan presents a way that the States can achieve this and return to financial stability.

13.2 Scenario 3 further enables the States to invest in much needed capital infrastructure and critical services to be able to meet the future demands of the Island and address the historic backlog. Critically it also ensures that cash reserves are maintained at a sufficient level to provide financial security, both now and for the future.

13.3 While Scenarios 1 and 2 provide an affordable option for the short-term they do not provide a sustainable position for the medium term or address the underlying fiscal deficit. They will, however, leave sufficient cash balances for the start of next term when urgent attention would need to be given to formalising and agreeing a clear plan to return to a sound and sustainable financial position.

13.4 The Policy & Resources Committee has the duty to advise the States on their financial resources, fiscal policy and economic affairs therefore believe it has no option but to recommend a solution that meets the needs of the Island in the medium to long term, rather than a short-term fix that fails to address the underlying issue. To do otherwise would be to fail to deliver against its mandate. It is for this reason that the Committee feels duty bound once again to ask the States to support a package of measures outlined in Scenario 3 that will deliver on the requirement to achieve long-term permanent balance and deliver urgently needed housing, education and health facilities.

14. Compliance with Rule 4

14.1 Rule 4 of the Rules of Procedure of the States of Deliberation and their Committees sets out the information which must be included in, or appended to, motions laid before the States.

14.2 In accordance with Rule 4(1)

a) The Propositions contribute to the States' objectives and policy plans and have been developed in line with the Government Work Plan priorities.

b) In preparing the Propositions consultation has been undertaken with all Principal Committees. In addition, all States Members have been offered the opportunity to input and there has been engagement with industry and union representatives.

c) The Propositions have been submitted to His Majesty's Procurer for advice on any legal or constitutional implications.

d) The financial implications to the States of carrying the proposals into effect are presented in this Policy Letter.

In accordance with Rule 4(2)

a) The Propositions relate to the Committee's responsibilities to advise the States and to develop and implement policies and programmes relating to fiscal policy, economic affairs and the financial and other resources of the States.

b) The Propositions have the unanimous support of the Committee.

Yours faithfully

PTR Ferbrache
President

MAJ Helyar
Vice President

JP Le Tocq
DJ Mahoney
RC Murray

ANNEX 1: FUNDING & INVESTMENT PLAN UPDATE

1. Summary

1.1 The Funding & Investment Plan (F&I Plan) is an integral part of the Government Work Plan (GWP), setting out the financial planning framework within which the States will operate and resource. The Plan covers all aspects of income and expenditure as known at the time of preparation (August 2023), augmented by best estimates based on informed assumptions to forecast future outcomes. It is not a firm plan of what will happen over the period but rather illustrates likely outcomes based on the key assumptions.

1.2 As stated in the original F&I Plan the aim is to provide a financial framework within which the States can operate. It does not replace the annual budgeting cycle through which budgets will be allocated or substitute the need for detailed investment appraisals to ascertain value for money and other benefits ahead of funding approvals.

1.3 In the 12 months since the last F&I Plan update there have been some significant changes to the States' priorities. The States agreed in the recent Tax Review debate at the beginning of 2023 that the longer-term financial position of the States of Guernsey is unsustainable. This debate concluded with no agreement to take forward any of the proposed tax packages to address the growing structural deficit. However, the States did agree a series of workstreams to look at revenue raising including vehicle ownership taxes, corporate taxes and visitor taxes. The States also agreed to cost-saving measures and for a full review of the capital portfolio, both with the primary aim of reducing States' spend.

1.4 Originally the F&I Plan was designed as the financial planning framework for the current term of government and therefore spanned the five years from 2021 to 2025. The first update in 2022 focused on year-on-year change with the inclusion of 2021 actuals. In this update, in light of the recent tax debate and the current financial environment, there is a strong focus on financing and affordability, but most importantly it proposes a path to long term financial sustainability.

1.5 The timeframe for the F&I Plan has been extended to 2032 to be able appropriately to assess funding sources and affordability in the next ten years. This Plan sets out measures that can be taken to bring Guernsey's finances back to a sustainable position in the longer term.

Outcomes from the Tax Review

1.6 In the Tax Review debate in February 2023, the States agreed that the longer-term financial position of the States of Guernsey is unsustainable, although no agreement was reached on any of the proposed packages seeking to address the growing structural deficit.

1.7 The States resolved:

"To agree that the longer-term financial position of the States of Guernsey is unsustainable and effective measures must be implemented in a staged approach to mitigate the challenges, particularly those arising from an aging demographic with increased health and care needs, requiring:

i. delivery of expenditure restraint, savings and revenue raising;
ii. the identification of a longer-term vision for Guernsey and an accompanying economic, social and environmental model;
iii. the consideration of alternative funding models for capital projects;
iv. the development and delivery of revised health and care models;

and to agree that the work associated with this issue is a very high priority for government and resources need to be re-prioritised accordingly."

1.8 Items i) and iii) of this Resolution are being tackled both through other Resolutions from the same debate and this policy letter. Item iv) has now been prioritised as one of the three strategic portfolios within the GWP with funding allocated.

1.9 With respect to item ii) preparatory work has started on this workstream. and the plan for completion is discussed in the GWP Workplan Policy Letter[1]

1.10 As one of the measures to deal with item i) above, the States resolved to set up a Sub-Committee to look into cost reductions:

"Direct the Policy & Resources Committee to establish a Sub-Committee working with Principal Committees, the States' Trading Supervisory Board and wider States Members, and after effective engagement with the community, to identify and review essential community services and to consider whether structural change, cessation, outsourcing and/or commissioning of those services could deliver significant savings having regard to:

i. the relevance of universal offers in the provision of services;

[1] Government Work Plan 2023-25

   ii. *value for money and the opportunities for potential efficiencies in service delivery;*
   iii. *the operating models for the States' trading assets;*

and to incorporate these into a medium-term plan for delivering overall cost reductions of at least £10m-£16m over five years to be considered by the States by the end of 2024."

1.11 A Sub-Committee has since been created to identify medium term cost control opportunities and will be reporting back to the States by Summer 2024 so that any proposals can be included in the 2025 Budget.

1.12 The Cost Saving Sub-Committee is well under way in its work with several initial steps taken including:

- Engagement with Committees for ideas on ways to reduce costs for their service areas, followed up with a review meeting and shortlisting activity.

- Three surveys developed and launched to the public; States employees; and Deputies to seek suggestions of further cost savings initiatives. These surveys generated over 2,000 ideas, which are now being reviewed and shortlisted.

1.13 In the meantime (i.e. ahead of the 2025 Budget), the Committee wished to ensure measures were being put in place to control costs. During 2023, efforts are being made to control revenue expenditure by pausing the release of funding from the Budget Reserve on new GWP initiatives or Service Developments except in exceptional circumstances.

1.14 For the 2024 Budget the Committee has set the objective that it be built on a no real-terms growth in net expenditure basis.

1.15 The terms of the 2024 pay award for States staff have already been agreed, which is set at RPIX-1% (at the reference date of June 2023 RPIX) giving rise to a pay award of 5.8%. This presents a significant challenge as inflation is projected to fall sharply in the second half of 2023 and into 2024, with the inflation forecast for the 2024 Budget for expenditure set at 5.5% overall (based on the forecast inflation rate at the end of 2023). Therefore, to contain overall budget growth within the 5.5%, Committees have been asked to prepare their budgets on a real-terms reduction of 2.5%. The only exception to this is the Committee *for* Health & Social Care, which has a target of no real-terms growth overall given the known demand pressures in that area. At the time of writing, only two Committee budget submissions have met or improved upon the target, with other Committees requesting budgets higher than the proposed cash limits. The Policy

& Resources Committee is in the process of reviewing these submissions with Committees.

1.16 A further Resolution was agreed to review the capital portfolio:

"Direct the Policy & Resources Committee through engagement with Principal Committees and wider States' Members to review the capital portfolio and pipeline in light of the outcome of the debate and report back to the States by March 2024 with recommendations for:

i. any changes to the scope or funding of the existing portfolio;
ii. alternative funding mechanisms including borrowing; and
iii. (if in the view of the Policy & Resources Committee thought appropriate) amending the assumption for the level of capital expenditure contained within Principle 6 of the Fiscal Policy Framework."

1.17 While the intention was for the review to be completed by March 2024, the Policy & Resources Committee decided to accelerate the review of the existing capital portfolio and its funding given the number of schemes that were due to come forward for funding post the tax review debate.

1.18 This review is aligned with the intention set out in the 2021 F&I Plan which stated the requirement for the capital portfolio to be reviewed regularly to ensure that the portfolio remains balanced, affordable and importantly deliverable by both the States internal resources and the on-Island construction sector.

1.19 The deadline was therefore brought forward to be in line with this F&I Plan update, enabling the States to consider the capital portfolio alongside the strategic priorities of the States and the States' finances in one sitting, as those decisions are inextricably linked as they respond to the pressures in our community and the wider context.

1.20 Once the initial review had been completed, the Committee suggested a reduced portfolio based on deliverability and affordability constraints and commenced consultation with Principal Committees on that proposal. However, during engagement strong views have been put forward on the urgent need for schemes that the Committee was proposing to delay. The detail around this review and the Committee's proposals can be found within Annex 2, and the funding of the proposed portfolio is addressed within this F&I Plan.

1.21 While the review has taken place, additional capital spending has been paused, other than for essential items that could not be delayed and for spend that would not be of no value should the substantive project not be accepted into the capital portfolio.

1.22 Resolution 9 from the debate directed the Policy & Resources Committee to:

"establish a sub-group to take forward the work on the investigation of changes to the tax system, with terms of reference as set out in the attached schedule and to report back with proposals and recommendations as work progresses"

1.23 This group has been established as a Sub-Committee of the Policy & Resources Committee and is systematically working through the items set out in the terms of reference. It has already made recommendations to the Committee for changes that will be put forward as part of the 2024 Budget. Further details on progress can be found in sections 11.32 to 11.44.

1.24 Although there are several other Resolutions which are being progressed by the Committee in line with the direction of the States, the final one of relevance to this report is the direction provided to the Committee, working with the Committee *for the* Environment & Infrastructure, to:

"*investigate annual revenues generated through transport, such work to include consideration of fuel duty, distance charging, the application of an annual tax on ownership of vehicles and paid public parking and to report back to the States by the end of March 2024*."

1.25 Following discussion between the Presidents of the two Committees, who agree that there is significant scope for generating additional revenues in this area, it has been decided to prioritise work on the introduction of an annual tax on ownership of vehicles.

1.26 Work is currently under way to review the potential collection mechanism and structure of such a tax and a substantive update is likely to be included in the 2024 Budget.

Economic Context

1.27 This F&I Plan update is presented at a turning point. The high level of inflation seen throughout 2022 has now begun to fall in Guernsey, albeit more slowly than had been forecast. This trend is set to continue with current forecasts projecting RPIX to fall below 5% in the first half of 2024 and, barring any more unforeseen shocks, fall further towards a more typical level later in the year.

1.28 As an effort to control inflation there has been a sharp increase in the Bank of England's base rate. After a decade of ultra-low rates, the base rate has risen rapidly back up to levels which are much more typical in the long term. That has been painful for borrowers, in particular those on variable rate mortgages, exiting fixed rate agreements or seeking new loans. Inevitably, the rising interest rates have slowed the property market as the affordability criteria on new mortgages has tightened. There has been a marked decline in the number of transactions taking place and average prices have also begun to fall.

1.29 While interest rates will eventually fall again, it is worth noting that the current 5% is more in line with long term norms than the sub 1% rates experienced since the 2008/9 financial crisis. It is unlikely that rates will fall back to this level unless there is another significant crisis.

1.30 Despite the ageing of the workforce, total employment has continued to grow through 2022 and into 2023, boosted by higher-than-average levels of net migration. This suggests that conditions in the economy and the labour market are strong. Ordinarily this would be reflected in real earnings growth, but earnings have lagged behind inflation since early 2022 owing to the speed at which inflation increased during this period. If the demand for labour remains strong, the opposite may happen as inflation rates fall. Wage negotiations, which are typically based on inflation rates reflecting the previous 12 months, and recruitment in a competitive labour market should make up at least some of the real value lost.

Strategic Context

1.31 In July this year the States debated the Government Work Plan 2023-25: the mid-term reset[2] and agreed (inter alia):

i. *"The general principle of three strategic portfolios for the duration of this political term, and that the Policy & Resources Committee will revert to the Assembly no later than September 2023 with Committee work plans that deliver:*

a. Public service resilience, security and governance;
b. Plan for sustainable health and care services; and
c. Grow economic competitiveness;

And to agree that the Policy & Resources Committee should take account of the associated costs, as far as is affordable, when recommending the Annual Budgets for 2024 and 2025.

ii. *That the Government Work Plan must be both affordable and deliverable and given that the costs for the delivery of States' extant and proposed strategies and services cannot be sustained, to note that the Policy & Resources Committee intends to revert to the Assembly no later than September 2023 with detailed funding proposals to ensure the Bailiwick's*

[2] Billet d'État XI, 2023

essential service, policy and infrastructure requirements are secure going forward."

1.32 As part of this reset, committees have estimated the cost of priorities within each strategic portfolio within their mandates and these have been included in this F&I Plan. While this plan includes the estimated costs, this does not mean that funding for these initiatives is approved. Appropriately detailed investment appraisals to ascertain value for money and other benefits will still be required ahead of funding approvals.

1.33 The current capital portfolio was agreed alongside the initial GWP in 2021, with a full prioritisation exercise aligned with Government's strategic aims. In line with the Resolution from the Tax Review debate to review the capital portfolio, revised and updated scenarios are presented as part of this Plan taking into consideration the strategic direction as set out in the GWP as well as affordability and deliverability constraints.

2. Objective of this Funding & Investment Plan

2.1 The objective of this F&I Plan is to present an achievable financial plan for the States of Guernsey. To achieve financial sustainability, it includes recommendations on borrowing to ensure adequate liquidity while funding the immediate priorities of the States.

2.2 What does a sustainable financial position look like? A long-term sustainable position of permanent balance would mean generating an ongoing revenue surplus sufficient to afford necessary capital and transformation projects (regardless of whether they are funded through in-year surpluses, reserves or borrowing) as well as covering the expenditure of the agreed strategic policies of government and ensuring reserves are sufficient. In the short term it means that the States of Guernsey have sufficient liquidity to ensure that the priorities of government can continue.

2.3 The F&I Plan also considers the Fiscal Framework, which is a set of principles agreed by the States to govern how they manage public finances. They commit the States to a guiding principle of permanent balance, which means that in the long-term government should not spend more than it collects. The Framework also states that any deficit should be addressed within five years and the temporary deficit should not exceed 3% of GDP.

2.4 Unlike the UK, the States of Guernsey are not a monetary authority. There is no central bank through which they can control monetary policy. A nation with this ability, such as the UK with the Bank of England or the USA with the Federal Reserve, can influence economic activity by manipulating the supply of money, credit and changing interest rates.

2.5 Guernsey is unable to do this, and it is therefore critical that the States manage island finances in a way that is sustainable.

2.6 In January 2023 Standard and Poor's Global Ratings (S&P) downgraded Guernsey's sovereign credit rating based on "*Guernsey's fiscal deficits and drawdowns from its financial assets"* further noting *"At the same time, global market turmoil has eroded Guernsey's significant asset buffer, which we estimate fell to 85% of GDP at the end of 2022".*

2.7 The report produced by S&P spanned four years from 2022 to 2026 and anticipated that Guernsey would likely push ahead with its significant capital spending programme despite forecast elevated deficits over this period. A key driver for the downgrade from an AA- rating to A+ was the significant erosion of cash reserves, which S&P had estimated fell to 85% of GDP in 2022 from a previous asset buffer of over 100%.

2.8 It was further reported that:

"*increasing pressure on health and care services is intensifying the squeeze on public finances, while the shrinking working age population also threatens tax collections*". The report included a warning of further "*negative rating action... if the government failed to implement tax reforms that stabilise its funding needs*."

2.9 In short, the States cannot continue to spend more money than they bring in and need to have a plan to return to a financially sustainable position in the medium term. However, in the short-term liquidity must be maintained, not only from a credit ratings perspective, but most importantly for financial stability. Should the credit rating be downgraded any further, taking out new debt would become more expensive, be on less favourable terms, and Guernsey could find itself in a position of being unable to afford essential projects or to run key services.

2.10 Previous ratings downgrades have generally been triggered either by technical changes in the evaluation criteria, or external factors (such as the UK's exit from the European Union) and have applied equally to competitor jurisdictions. The latest downgrade was the first purely on the basis of a worsening in the States' financial stability and has led to a differential with other similar jurisdictions. The Committee strongly believes that it is important to stabilise this position and not be subject to a further downgrade which would widen the gap between Guernsey and similar jurisdictions.

3. The F&I Plan and the GWP Priorities

3.1 The 2023 update to the F&I Plan began with the Committee engaging with all Principal Committees requesting a review of their GWP priorities with the aim of reducing activity to that which was necessary and deliverable only.

3.2 In addition to this, in March 2023 the Committee wrote to all Principal Committees requesting that they curtail GWP expenditure for 2023 with immediate effect until consideration was given to funding.

3.3 Each Committee undertook a full review of the applicable GWP priorities to explore what initiatives could be put on hold, or stopped, and what needed to be progressed.

3.4 The Committee held meetings with each Principal Committee and the States' Trading Supervisory Board (STSB) to discuss the capital portfolio and GWP reset, outlining the affordability and deliverability constraints.

3.5 Committees were requested to write formally to the Policy & Resources Committee with their views, which were then incorporated into the GWP reset and the development of the capital portfolio scenarios. Further detail on the capital portfolio, the review and proposed options is in Annex 2.

4. Funding & Investment Plan compared to 2022 Published Accounts

4.1 Financial accounts, as useful as they are, aren't the only source of information for financial decision making, planning and management. The accounts have a historic focus and provide a snapshot of the assets at the end of the year, which doesn't necessarily provide the information required for future decisions on the funding and financing of States priorities. Planning of this type requires a different type of financial analysis and because of this the F&I Plan uses the 2021 and 2022 accounts but makes specific adjustments to aid decision making.

<u>Surplus/Deficit</u>

4.2 The table below (table 1) shows how the surplus or deficit reported in the 2022 States of Guernsey Accounts reconcile back to the F&I Plan baseline surplus, which includes General Revenue income and expenditure only.

4.3 Some of the reconciling adjustments remove non-General Revenue items, such as investment returns and interest on the Core Investment Reserve.

4.4 The reconciliation adjusts for the Contributory Funds in 2022 when they were included in the States of Guernsey Accounts for the first time. However, the F&I Plan does include the contributory funds surplus/deficit within the "Overall Funding Requirement" in section 10 of this report.

4.5 Non-cash accounting items, such as revaluation of investment property, have also been adjusted out of the projections as these are not relevant to the funding requirement, which is the prime focus of this F&I Plan.

4.6 Accounting entries relating to capital have been adjusted as capital expenditure is captured separately in the F&I Plan to allow a clearer understanding of the funding requirement and affordability.

Table 1: Reconciliation of the Accounting Surplus/Loss to the F&I Plan

	2021	2022
	£'m	£'m
Published accounts surplus /(deficit)	**£48**	**(£135)**
Contributory Funds deficit	£0	£14
External interest receivable (other SOG funds)	(£6)	(£6)
Investment loss/(return) on (other SOG funds)	(£29)	£22
Finance Charges (other SOG funds)	£11	£11
Depreciation Charges	£29	£29
Capital expenditure expensed in year	£14	£19
Loss/(gain) on revaluation of investment property	(£2)	£0
Write Down of Incorporated Trading Entity Carrying Balance	£47	£12
Adjustment for impairment of short-term loan facilities provided to trading entities	(£22)	(£14)
Balance of seized asset fund transferred from depositor account	(£17)	0
Contribution to related parties	(£5)	(£2)
Other	(£2)	£1
F&I plan Operating Surplus/Deficit *	**£66**	**(£49)**
Capital Spend	£40	£45
F&I plan Net Surplus/Deficit including Investment returns	**£26**	**(£94)**
F&I plan Net Surplus/Deficit before Investment returns	*(£22)*	*(£19)*

** General Revenue only.*

Reserves

4.7 The 2022 States of Guernsey Accounts report a total accounting reserves balance of £3.3bn as at the end 2022.

4.8 This includes the Core Investment Reserve (£158m), the States Trading Entities Reserve (£113m) and the balance of the Contributory Fund Reserves; the Guernsey Insurance Fund (£720m) and the Long-Term Care Insurance Fund (£129m). None of these reserves can be used for funding the priorities of

Government as they are ringfenced through policy, legislation, or are accounting reserves only and are therefore not included in the F&I Plan financial projections.

4.9 The 2022 Accounts also report £1.7m in the Fixed Asset Recognition Reserve, which was created when the States adopted IPSAS (International Public Sector Accounting Standards) fixed asset accounting. The onboarding of assets necessitated the creation of a new reserve but this does not represent available funding and is therefore not included in the F&I Plan.

4.10 The F&I Plan only includes the available reserves that can be used to fund the priorities of this or future Governments.

Capital and Transformation Spend

4.11 In 2022 £45m was spent on capital portfolio projects (with an additional £14m spent on transformation projects) and comprised of £31m of major capital and £14m of minor capital expenditure on the everyday replacement of equipment and vehicles, renewal of roads and investment in property assets.

4.12 As part of the transition to asset accounting in 2022 there was a review of capital expenditure, as only the spend which qualifies as capital under IPSAS could be added to the asset register and accounted for as capital expenditure.

4.13 Following this review, it was determined that £14m of the 2022 major and minor capital spend could not be capitalised and was therefore accounted for as revenue expenditure. In addition, some project costs incurred by the States of Guernsey on behalf of related parties were accounted for as revenue expenditure, an example of this are the grants paid to the Guernsey Housing Association as part of the Affordable Housing Programme prioritised within the major capital portfolio. The total cost that was added to the States of Guernsey asset register net of these adjustments was £23m in 2022.

4.14 2022 was the first time that depreciation was included in the accounts with a charge of £29m in that year. This relatively low amount when compared to the F&I Plan projected capital expenditure is a result of the following:

a) Firstly, the historic lack of investment in infrastructure, which has resulted in a sizeable number of assets now past their useful life and are no longer being depreciated. As States investment in assets increases so too will the depreciation charge.

b) Secondly, depreciation is purely for capitalised assets. There will be expenditure on projects within capital and transformation portfolios that do not result in the creation of an asset but are essential to reorganise services and deliver benefits. In 2022 there was £28m of such expenditure (£14m on transformation and £14m on projects in the capital portfolio). The combined total of this written-off spend and depreciation equates to an amount equivalent to 1.7% of GDP, only slightly below the 2% GDP target as per the Fiscal Policy Framework (see Appendix 6).

5. Financial Performance Update 2021-22

5.1 The 2022 F&I Plan update described the better than anticipated results from the initial 2021 Plan. The actuals in 2021 were £61m better than the F&I Plan mainly due to the following:

a) Income tax recovered to pre-COVID-19 levels much faster than anticipated and accounted for £17m of the improvement.

b) Document Duty was £11m better than estimated largely due to significantly higher residential property prices, despite a large increase in receipts between 2019 and 2020 from both volume and value of property sales reflected in the F&I Plan.

c) The net impact of the pandemic on Customs Duty saw an increase of £6m against the F&I Plan. Whilst lockdown meant that fuel duty dropped, this was more than offset by continued high levels of income from tobacco and alcohol sales as a result of restricted travel limiting accessibility to duty free purchases.

d) Expenditure decreased against the F&I Plan by £24m and was largely considered one-off due to ongoing effects of the pandemic. Resources were diverted away from planned activity in the Principal Committees resulting in limited service and delays to service developments. The Budget Reserve was underspent as pay awards cost less than forecast and the full amount set aside for COVID-19 related costs (mainly vaccination and testing) was not required.

e) In addition, investment returns in 2021 were £28m higher than forecast. Higher income, lower expenditure and a slower rate of investment in infrastructure throughout 2021 meant that cash reserves were higher than expected throughout the year. Not only was this increased balance able to be invested, but this was also combined with it being an excellent year for investments with a return of 9.7% achieved.

5.2 Many of the reasons behind this positive outturn for 2021 were exceptional, linked to the pandemic, and did not continue into 2022.

5.3 The 2022 F&I Plan update figures were based on a forecast, rather than budget, but still there were some significant changes. The key differences between the actual 2022 result and the F&I Plan were:

a) Revenue performed nearly 4% better than expected, with positive performance across most revenue income categories. Income tax receipts increased through wage inflation and an increase in the number of people employed. Document Duty was lower than 2021, as expected, but still higher than the 2022 estimate.

b) Revenue expenditure was approximately 2% higher than expected, driven by recruitment challenges particularly in Health & Social Care.

c) The net investment return was expected to be a gain of £46m in 2022, instead a loss of almost £73m was returned. This was a significant swing from 2021 and demonstrates the variability that can be expected from investments that are held long-term and is especially stark when looking at the difference between these two years.

5.4 The F&I Plan for 2023 has been updated to include actual figures for 2021 and 2022.

6. Forward Looking - Funding & Investment Plan Scenarios

6.1 This F&I Plan presents three scenarios for the financial performance of the States as well as a baseline, for comparative purposes only. Each scenario has an accompanying capital option based on its affordability and priority as set out in the capital portfolio review in Annex 2.

Baseline

6.2 This shows the projected financial position of continuing "as is" and assumes all actions previously prioritised within the GWP progress as planned, albeit at the most up-to-date cost estimates. The baseline shows the financial impact of taking no further action with regards to cost saving or income raising initiatives and is the position against which the proposed scenarios can be compared.

6.3 The baseline assumes that the capital portfolio continues as originally prioritised in the 2021 GWP, but latest costs and phasing have been applied to the cashflow requirements.

6.4 The baseline is for comparative purposes only. It is not a valid option and the States have already resolved that it is not possible to continue on the current trajectory.

Core Elements

6.5 This section details the core elements inherent to all 3 scenarios.

i. Income measures – limited additional revenues including the implementation of pillar 2 corporate tax measures (see paragraph 11.33 for more details) and other corporate tax initiatives, an annual charge on vehicle ownership and other transport related taxes and visitor taxes. The total revenues forecast to be generated are estimated at £25m per annum.

ii. Expenditure savings - £10m of recurring annual savings implemented incrementally over 5 years.

iii. Investing in policy development – covers the prioritised GWP policy initiatives plus assumes an additional £3m made available each term for future policy development.

iv. Core 'in-flight' capital projects – these schemes have already had substantive investment, are being delivered or are near completion and funding is therefore committed. There are 17 projects in this category that require funding of £96m in total.

Scenario 1

6.6 Scenario 1 includes the core elements detailed above plus a further £94m for the major capital portfolio. This limited capital portfolio is set at a level that ensures this scenario remains affordable in the short to medium term and that cash reserves are protected.

6.7 Total funds available to the capital portfolio for this political term's priorities have been reduced to £190m from 1 January 2023 to scheme completion. This excludes minor capital funding of £20m per year and costs for transformation.

6.8 Capital expenditure for future political terms is projected at 2% of GDP per annum.

Scenario 2

6.9 In addition to the core elements this scenario includes new borrowings of £200m to help fund the capital portfolio.

6.10 Furthermore, in this scenario the Health Service Reserve is used towards funding the hospital modernisation project.

6.11 The result is a larger capital portfolio with £440m of funds available to this term's capital portfolio from 1 January 2023.

6.12 Capital expenditure for future political terms is projected at 2% of GDP per annum.

Scenario 3

6.13 In addition to the core elements this scenario models the implementation of the full progressive tax package as previously debated in early 2023.

9.13 New borrowings of £350m are assumed, allowing further funds to be made available to this term's capital portfolio ahead of the new revenue raising being implemented.

9.13 The funds available for this term's capital portfolio from 1 January 2023 onwards are capped at £520m, with capital expenditure projected at 2% of GDP from 2026 onwards.

6.14 Further details of the capital portfolio for each scenario can be found in Annex 2 and Appendix 5.

7. Key Modelling Assumptions

Core Assumptions Common to all Scenarios

7.1 The Plan has been updated with the 2022 actual income and expenditure and estimates for 2023 to 2033 based on latest projections and forecasts.

7.2 Inflation is included within the financial projections at the following rates:

Year	Rate
2023	5.5%
2024	3.5%
2025 +	2.5%

7.3 Prior year actuals are shown as the actual figures and are not inflated.

Revenue Assumptions

7.4 Based on historic performance real (above inflation) GDP growth is assumed at 0% for 2023 due to high inflation levels and 0.5%-0.6% per year 2024 and beyond (with a similar assumption of median earnings growth).

7.5 Demographic changes including the ageing of the population is inherent in the GDP projections and feeds through to income projections for tax and social security contributions and costs.

7.6 The programme of continuation of the increase in social security contributions as agreed by the States in October 2021, following consideration of the report entitled 'Contributory Benefits and Contributions rates for 2022'[3], has been included for all scenarios other than Scenario 3. The States have approved plans to increase the percentage contribution rates to the Guernsey Insurance Fund (GIF) over ten years and the Long-Term Care Insurance Fund (LTCIF) over four years. This could be replaced by a restructured system of contributions raising an equivalent amount of revenue.

7.7 Large cyclical boosts from the banking sector for 2022 are not forecast to continue through 2023 and the forecast outrun and projects for all subsequent years reflect this.

7.8 The long-term average net migration is assumed to be +150 people per annum. While the agreed policy objective supports a higher level of net migration, this is yet to translate into practical application and housing supply is expected to be a limiting factor. The F&I Plan assumption is therefore based on historic averages; however, the impact of a higher or lower rate is explored in the sensitivity analysis (Section 16). It should be noted that +150 net migration is not enough to maintain our work force at its current size long term. To maintain the workforce at current levels, net migration would need to rise to approximately +300 people a year. However, with the phased increase in the pension age to 70 by 2049, the reduction in workforce does not become noticeable until the end of the F&I Plan projection period.

7.9 A higher assumption of net migration has been included in 2023 because recent net migration (up to Sept 2022) has been higher than average.

7.10 TRP is assumed to grow at +1% in real terms before any tax measures due to expected growth in housing stock.

7.11 2023 saw a £14m contraction in document duty from a peak in 2022 (£32m) because of the sudden slow-down in transaction numbers and a fall in prices as interest rates have risen. To smooth these cyclical effects, document duty forecasts have been rebased to the ten-year average (adjusting from movements in prices) of £25-26m. The long-term assumption is for +1% growth in real terms reflecting a slower increase in prices and tailing of demand following high activity in recent years. Document duty is inherently difficult to forecast as it is

[3] Billet d'État XX 2021

dependent on both the volume and value of conveyances; cyclical impacts are likely and as a result the document duty forecast is particularly volatile.

7.12 For Customs and Excise duties the assumption is that any real terms increases will be offset by a continuing 2% per annum loss of fuel volumes.

7.13 Company fees have been modelled with an assumption of +0.7% real terms growth aligned with average economic growth and reflecting an expectation that growth will be focused in sectors subject to 10% and 20% tax rates.

7.14 The estimated impact of secondary pensions on income tax has been calculated and included in the projections. Secondary pensions will reduce taxable income initially as tax relief is provided on pension contributions. As enrolments and contributions into the scheme grow the impact on income tax increases. This will plateau towards the end of the 10-year period that this forecast covers and in the longer term will result in a positive financial benefit to the States as pensions are drawn and become taxable.

7.15 An additional real terms increase of £1m per annum of budgetary revenue raising measures is assumed for the full ten years of the forecast. This will mean that real-terms increases in customs duties and/or TRP will be necessary in future annual budgets.

Expenditure Assumptions

7.16 2023 reflects the authorised budget for this year, adjusted for pay awards settled post budget publication.

7.17 Transformation expenditure, which was part of the 2023 General Revenue Budget, is not included in these committee expenditure projections, but is included as a separate item in the F&I Plan within “Capital & Transformation Spend”.

7.18 The forward projections include an estimate for above inflation pay awards (0.5%) in line with the long-term average.

7.19 A £5m Budget Reserve has been incorporated in addition to committee estimates each year. Historically, a contingency of approximately £5m has been included in the annual Budget to manage overall budget contingencies and deal with any one-off, unexpected, or in-year cost pressures such as variations in formula-led expenditure, increase in cost or demand for services in excess of that included in the Cash Limits and a limited amount of funding for other unanticipated/contingency/’emergency’ expenditure where there is a clear business case to justify it.

7.20 The baseline has factored in the increasing demand for healthcare. While this is hard to predict with any degree of certainty, recent modelling that takes into account demographic and non-demographic demand growth, capacity issues, and off-Island provision has highlighted a potential for costs to increase by 1.3% - 1.4% per annum to 2040 (a real terms increase of 34% by 2040). Based on this modelling a provisional amount of an additional £4.0m has been included per annum from 2024-2032.

7.21 This forecast is based on the current service delivery model for Health and current service offering. Any change to services could result in additional costs over what has been forecast. For example, the model of care and potential funding mechanisms under SLAWS (Supported Living and Ageing Well Strategy) which will be debated in early 2024 may result in additional costs over what has been modelled.

7.22 In addition, budget pressures identified by the Committee *for* Heath & Social Care (C*f*HSC) as part of the 2023 budget setting related to staff accommodation and higher than usual off Island costs part driven by COVID-19, have been assumed to continue at £2m per annum until 2025 then reduce to £1m from there onwards.

7.23 Based on advice from the PWC review conducted on the IT outage in 2022 an additional £1m per annum has been included for IT revenue expenditure to address identified issues. It has also been assumed that there are no further savings associated with the Future Digital Services (FDS) contract.

7.24 The Revenue Impact of Capital Expenditure (RICE) is based on the current approved portfolio.

<u>States' Trading Assets Funding Requirements</u>

7.25 The future potential funding requirements for the States' Trading Entities is currently being reviewed by the STSB as part of its review of Ports' operations, however, an estimated cost of £3m in 2023 and £1m per annum from 2024 to 2032 has been included to represent the estimated operational deficit of the Ports.

7.26 The Waste deficit is funded through General Revenue for 2023 and it has been assumed that £0.5m per annum is required from 2024 onwards.

7.27 No additional funding requirements have been included for the other incorporated and unincorporated trading assets. In summary:

- Aurigny is expected to break even

- The Dairy is assumed to break even
- It has been assumed that any surpluses generated by Guernsey Water and States Works can be invested in their infrastructure requirements.
- It has been assumed that there is no dividend from Guernsey Post or Guernsey Electricity.

Other Assumptions

7.28 Investment income is assumed at 2.5% above inflation. While this is less than the investment strategy target it represents a realistic estimate of actual performance. This is a long-term average assumption, but variability year-on-year is expected, as evidenced by the large swings in 2021 and 2022. The investment return to 30 June 2023 was 2.25% which is significantly below the target included in the model. See paragraphs 17.1 to 17.5 for further details.

7.29 An estimate for proceeds on disposal of fixed assets has been included at £3m for 2023 and £1m per year for 2024 onwards.

7.30 New long-term borrowing has been assumed at an interest rate of 5.5% with repayments over 30 years. This is based on a 0.80% spread on UK Gilts.

7.31 It has been assumed that the capital repayment of funds from the States of Guernsey Bond used to fund the capital portfolio are repaid to the Bond Reserve from 2026. Coupon costs have been charged to General Revenue from drawdown.

Baseline GWP (Strategic Portfolio) Cost Assumptions

7.32 The costs relating to GWP actions for this political term have been updated with the latest figures. It is assumed in the baseline model that the GWP priorities continue as planned but are updated with latest cost and phasing assumptions.

7.33 The costs of the updated GWP actions debated by the States of Deliberation on 18th July 2023, have been included in Scenarios 1-3.

7.34 An ongoing amount of £3m per year has been included from 2026 for the Strategic & Policy Portfolio (GWP) for future years' priorities. This is a high-level planning assumption only and future States may decide to spend more or less the £3m allowed for in this F&I Plan.

Baseline Capital Portfolio Assumptions

7.35 The baseline assumes the capital portfolio prioritised during the initial F&I Plan in 2021 is delivered according to latest deliverability and costing updates from the project leads.

7.36 Financial modelling also assumes investment for future terms' capital expenditure at 2% of GDP (to cover major, minor and transformation spend). This is in line with the agreed average capital expenditure in the Fiscal Policy Framework. It should be noted that, in line with the Fiscal Policy Framework definition, this target does not include the capital spending of the States' incorporated and unincorporated trading entities, given that these should operate as commercial entities.

7.37 Minor capital is projected at £20m per year (at 2023 prices) as a minimum necessary for each option.

Core Elements - Assumptions

7.38 In addition to the assumptions detailed above, the following applies to the core elements of each scenario:

a) An additional £10m per annum has been assumed from mid-2025 from transport-related taxes and charges.

b) Corporate taxes, including those from Pillar 2, are assumed at an additional £15m from 2026. Pillar 2 is part of the two-pillar solution to address the tax challenges arising from digitalisation of the economy included in the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS), to which Guernsey is a signatory. The application of Pillar 2 provides a co-ordinated system to ensure that Multinational Enterprises (MNEs) with revenues above EUR 750 million pay at least a minimum level of tax (15%) on the income arising in each of the jurisdictions in which they operate. Guernsey has made a joint statement with Jersey and the Isle of Man detailing their intention to implement legislation to meet the requirements of Pillar 2 from 2025, although revenues are not likely to be forthcoming until 2026 at the earliest. This will apply to a small number of qualifying MNEs and their subsidiaries located in Guernsey, and estimates suggest this will raise around £10m a year in local tax contributions. A further £5m is a result of other potential changes to corporate tax as being reviewed by the Tax Sub-Committee. Further details can be found in paragraphs 11.32 to 11.44.

c) Cumulative annual recurring savings are built into the scenario as follows:

- 2024 - £2.5m
- 2025 - £4.0m
- 2026 - £5.5m
- 2027 - £7.0m
- 2028 - £8.5m

- 2029 – £10.0m

d) There are 17 ‘in-flight’ capital projects included in ‘core’ that require funding of £96m in total. Full details of these schemes can be found in Appendix 5.

Scenario 1 Assumptions

7.39 In addition to the core assumptions, the following has been included for Scenario 1:

e) Updated GWP priorities as endorsed by the States at their Special Meeting on 18 July 2023 have been included. Following the review of the GWP priorities some activities were stopped and others rephased. However, there were also new priorities added, leading to an increase in cost overall. Since that debate the “Local Planning Briefs” action has been added to the GWP portfolio (this was previously included as a capital portfolio project). Further details on the GWP actions and cost can be found in appendix 10 of the GWP policy letter.[4]

f) The ongoing costs of those priorities which may result in future service developments have also been estimated and included. In addition, £3m ongoing cost per annum from 2026 has been included for the strategic priorities of future political terms.

g) The revenue impact of capital expenditure (RICE) has been based on delivering the projects prioritised in Portfolio 1.

Scenario 1 Capital Portfolio Assumptions

7.40 Scenario 1 assumes a much-reduced capital portfolio affordable in the medium term by using available funding with no additional borrowing.

7.41 In the longer-term, capital spend of 2% of GDP has been assumed each year.

7.42 Details on this option can be found in Annex 2 and Appendix 5, but in summary the following projects would be unaffordable under this scenario:

a) Transforming Education Programme – including the Les Ozouets Campus construction project to deliver an 11-18 education facility.
b) Our Hospital Modernisation Phase 2 – the remaining hospital redesign.
c) Alderney Airport Pavement Rehabilitation – to repair and extend the runway and modernisation of the terminal and other buildings.

[4] Government Work Plan 2023-2025

d) Bus Replacement – vehicles to support future public and education transport requirements.
e) SAP Roadmap – updating the organisation's systems including payroll, recruitment, and vendor management.
f) SMART Court – enabling more efficient services to be provided from the Greffe, HM Sheriff and Sergeant and Registrations department through digital and information technologies.
g) Future Inert Waste Facility

7.43 Reflecting the importance of housing, as well as flood defences to the Island, a new project "Bridge Regeneration Housing and Flood defences" has been added to the portfolio.

7.44 In addition to the baseline minor capital projection of £20m per year, in this scenario an additional £4m of funding has been included as an estimate of costs that may be incurred due to the delay of major capital schemes resulting in additional minor capital works.

7.45 Further, £5m (£1m per year for five years) has been included as a RICE cost assumption due to potential double handling costs as a result of a delay to the Future Inert Waste project. It should be noted that in all scenarios a double handling cost from 2024 has been built in, but this assumption assumes that the length of double handling is extended, owing to a delay in the project commencement.

7.46 There is no unforeseen provision in this scenario, which leads to the risk that the scenario becomes unaffordable if there is an unavoidable, urgent project.

7.47 The funding included to progress pipeline schemes is limited to £1m in this scenario, which would restrict the amount of development and early design work that can be progressed for a much greater number of projects.

Scenario 2

7.48 The key difference between Scenario 1 and 2 is that Scenario 2 includes borrowing in order to fund a larger capital portfolio, albeit this is still a reduction compared to the existing prioritised portfolio.

7.49 Borrowings are limited to what would be affordable under this scenario and are capped at an additional £200m in line with existing approvals from 2021.

7.50 In this scenario it is assumed that the Health Service Reserve is used to fund capital, up to the available funds from the reserve. As a result, it has been assumed the NICE TAs, which are currently funded from the Health Service Reserve, would be funded from General Revenue from the end of 2024. In all other scenarios these costs are assumed to continue to be funded from the Health Service Reserve until 2032, and, depending on the other uses of that reserve, potentially for up to a further 7 years.

7.51 RICE costs have been calculated based on delivering Portfolio 2 (see Appendix 5 for details of schemes).

Scenario 2 Capital Portfolio Assumptions

7.52 This portfolio builds on Portfolio 1 and is an evolution of that set out to Principal Committees in March 2023. Details of this option can be found in Annex 2, but in summary:

a) Our Hospital Modernisation Phase Two (OHM Phase 2) and the Transforming Education Programme (TEP) are classified as 'deliver as planned', with both programmes included at the current estimated costs.

b) Bus Fleet Replacement Phase 3 and SMART Court are included as 'do but review scope and / or solution'.

c) Alderney Airport Pavement Rehabilitation - to repair and extend the runway and modernisation of the terminal and other buildings (Option C+), is included as 'do as planned'.

d) SAP Roadmap - replacement of the Enterprise Resource Platform is still deemed unaffordable in this portfolio and remains as a pipeline project.

e) Future Inert Waste is still deemed unaffordable in this portfolio and remains as a pipeline project.

7.53 A cost of £3m (£1m per year for three years) has been included in the calculation of the RICE cost due to potential double handling as a result of a delay to the Inert Waste project. It is assumed that the delay would be shorter in this option, as there would be fewer projects remaining to be prioritised in the next political term.

7.54 The unforeseen projects provision in this scenario is £12.5m and the funding included to progress pipeline schemes is limited to £2.5m.

7.55 The assumption on minor capital is the same as Scenario 1 at £20m per year.

Scenario 3

7.56 This scenario includes the full tax package as presented to the Assembly in early 2023. The package includes the reform of social security contributions, the introduction of a lower rate of income tax for earnings up to £30,000 to make the tax system more progressive and a Goods and Service Tax (GST) which would either be set at 6% with food excluded or 5% with food included. The additional revenues generated from the tax package are split across the contributory funds and General Revenue reserve so that the contributory funds are not negatively impacted from the changes proposed.

7.57 RICE costs have been included in line with the projects prioritised in Portfolio 3.

7.58 In addition, it has been assumed that funds will be ringfenced for initiatives that have a social or community benefit. The details are still to be established but funds could be ringfenced for new arts or sports initiatives or for a "Green" fund. As an example, a green fund could be set up to assist homeowners with the cost of insulation or solar panels. Costs have been included at £5m for the remainder of this political term and £2.5m per year for the remainder of the modelling period.

7.59 This scenario also assumes new borrowing of £350m to enable further funds to be made available to the capital portfolio.

Scenario 3 Capital Portfolio Assumptions

7.60 A maximum amount of £520m is made available to the capital portfolio in this scenario, allowing the broadest range of investment across each of those presented in this F&I Plan.

7.61 This portfolio builds on Portfolio 2 and enables a continuation of the following projects as 'do as planned' at their full estimated investment levels:

a) Future Inert Waste Facility
b) SAP Roadmap

7.62 The 'unforeseen' provision in this scenario is £31m and the funding included to progress pipeline schemes is £5m.

7.63 The assumption on minor capital remains the same as in all scenarios at £20m per year.

Summary of Modelling Assumptions

7.64 It should be noted that all assumptions are made to enable the financial projections in this F&I Plan and are not reflective of any budget or agreed plan at this stage. Assumptions are based on best estimates of costs at the time and should not be taken to represent budgets or allocations of funding.

7.65 The modelling assumptions for each scenario are summarised in Appendix 2

8. Baseline Projections

8.1 The modelling assumptions described above in paragraphs 7.1 to 7.36 have been used to project a ten-year financial model. The chart below (Figure 1) shows the baseline projections i.e. the financial position based on where we are now if no further revenue raising or savings decisions are made.

8.2 This shows the overall funding requirement, or overall surplus or deficit in each year. This comprises the General Revenue position in addition to the contributory funds, plus estimated capital expenditure in the year.

8.3 The chart is shown both before and after financing activities. The blue line is before financing activities and is indicative of the underlying funding requirements, before investment return.

8.4 It is important to include investment return, as it contributes to the States' reserves, but it should be borne in mind that there is no positive cash impact until the underlying asset (the investment) is sold. The investments held by the States are relatively liquid; they can be bought and sold on financial markets, providing the States with the ability to convert them to cash relatively quickly. Investment returns are uncertain, however, and while our long-term average planning assumption of +2.5% above inflation is considered prudent, this can fluctuate significantly year on year, as seen in 2021 and 2022. Further, investment returns are dependent on the extent of reserves and therefore don't form part of the underlying position.

8.5 Throughout this document therefore the position is shown both before and after the inclusion of financing activities so that the underlying funding requirement can be seen clearly.

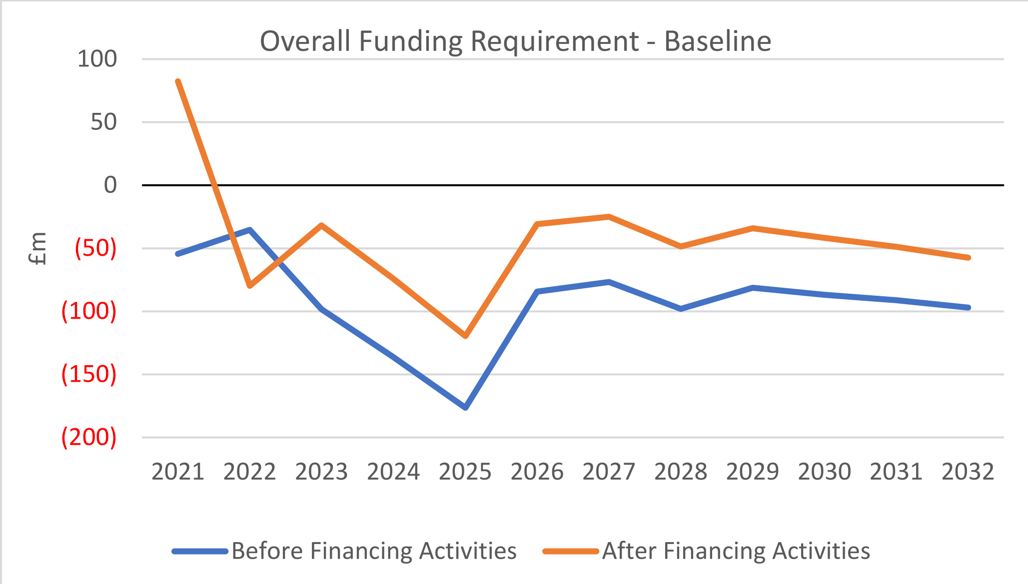


Figure 1

8.6 Figure 1 shows that the Baseline position is unsustainable. There is a projected overall deficit both before <u>and</u> after financing activities.

8.7 The chart shows a higher funding requirement in this political term which is projected to be as high as c£170m in 2025 as a result of the current capital portfolio, with the long-term requirement around £100m per year.

8.8 Figure 2 shows the same baseline for General Revenue only (without the contributory funds to enable visibility of the available cash to fund the capital portfolio) and the impact on reserves. This shows that the General Revenue surplus (General Revenue income less General Revenue expenditure) is significantly less than the projected spend on capital and transformation (the red line).

8.9 As a result, reserves deplete year on year and would be entirely depleted within a matter of years, meaning that by 2029 the States would need to borrow. However, it would be challenging to source the borrowing required at that stage with no means of affording it or reserves to fall back on.

8.10 While the capital and transformation projections are high in this political term because of the larger than usual capital programme, in the long term the capital is projected at 2% of GDP, and the chart shows that the General Revenue surplus remains too low to be able to afford the capital required.

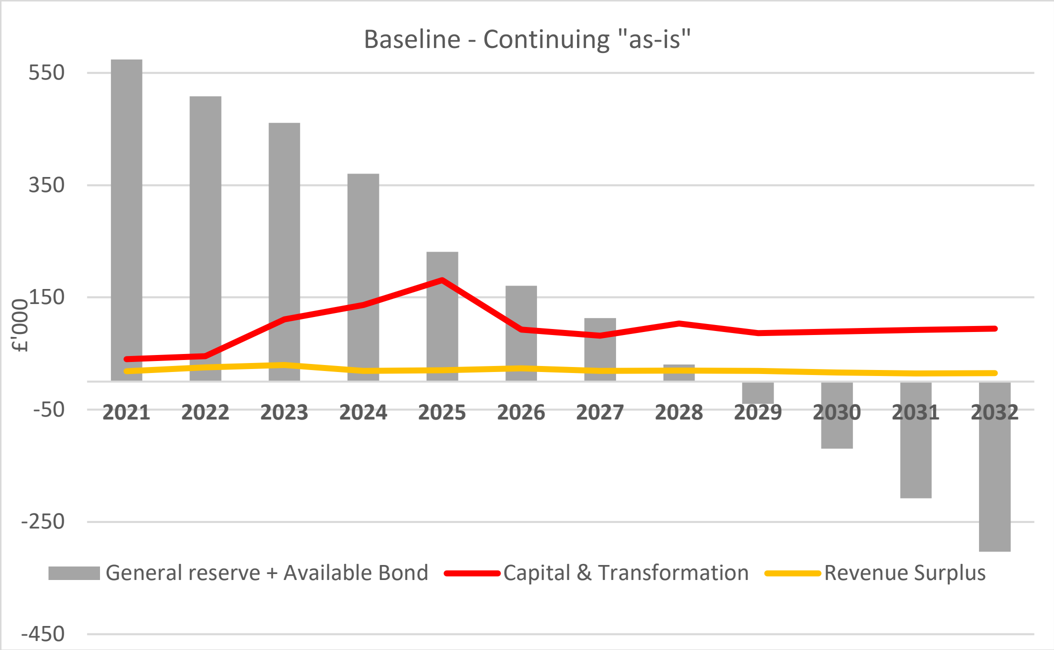


Figure 2

8.11 The baseline position is clearly unsustainable in the medium term and on an ongoing basis. This is in line with the Resolution made by the States of deliberation following the Tax debate in February 2023.

8.12 Following that debate the States resolved to agree that the longer-term financial position of the States of Guernsey is unsustainable and effective measures must be implemented in a staged approach to mitigate the challenges, particularly those arising from an ageing demographic with increased health and care needs. This clearly shows the short-term position in unsustainable.

9. Scenario Projections & Long-Term Sustainability

9.1 This section will discuss the long-term sustainability of the three scenarios modelled.

9.2 Projections have been extended beyond this political term to a ten-year horizon. While this may not be considered long term, the overall patterns can be identified, and they allow an assessment of financial sustainability. Owing to the increasing level of uncertainty inherent in longer projections, there would be little benefit in extending beyond this timeframe.

9.3 For this assessment a comparison is made between the projected revenue surpluses and the capital expenditure that the States should be investing in line with the Fiscal Policy Framework.

Principle 6 of the Fiscal Policy Framework (Capital Spend)

9.4 The agreed fiscal policy framework states:

"Principle 6: Total capital expenditure over any States term should be maintained at a level which reflects the need for long-and-medium-term investment in infrastructure and direct capital expenditure by the States should average no less than 1.5% of GDP per year averaged over a four-year period and 2% per year averaged over any 8-year period."

9.5 As part of the Tax review debate[5], the States resolved (inter alia):

To direct the Policy & Resources Committee to:

Review the Capital Portfolio and pipeline in light of the outcome of the debate and report back to the States by September 2023 with recommendations for

i. any changes to scope or funding of the existing portfolio; and
ii. (if in the view of the Policy & Resources Committee thought appropriate) **amending the assumption for the level of capital expenditure contained within Principle 6 of the Fiscal Policy Framework.**

9.6 A full review of Principle 6 is yet to be undertaken but the current capital portfolio equates to approximately 2.6% of GDP and in addition there is a large pipeline of projects.

9.7 Historically the spend has been lower than 2%, but as a result there is now a backlog of infrastructure replacement projects, suggesting that the historic spend was not sufficient and that reducing to below 2% could risk the investment in essential infrastructure being too low.

9.8 Notwithstanding the outcome of the full review that will be undertaken in due course, this suggests that 2% seems appropriate on a planning basis if we want to maintain our infrastructure to the required standard.

Scenarios: Long Term Sustainability

9.9 The chart below (figure 3) shows the 10-year revenue surplus forecast for each of the three scenarios. Note that this is before any financing activities (investment returns, debt interest expense etc) and before investment in capital expenditure (minor, major, transformation). These projections also exclude the social security deficit. This enables clear visibility of the funding available for capital expenditure.

[5] Billet d'État III, 15th February 2023

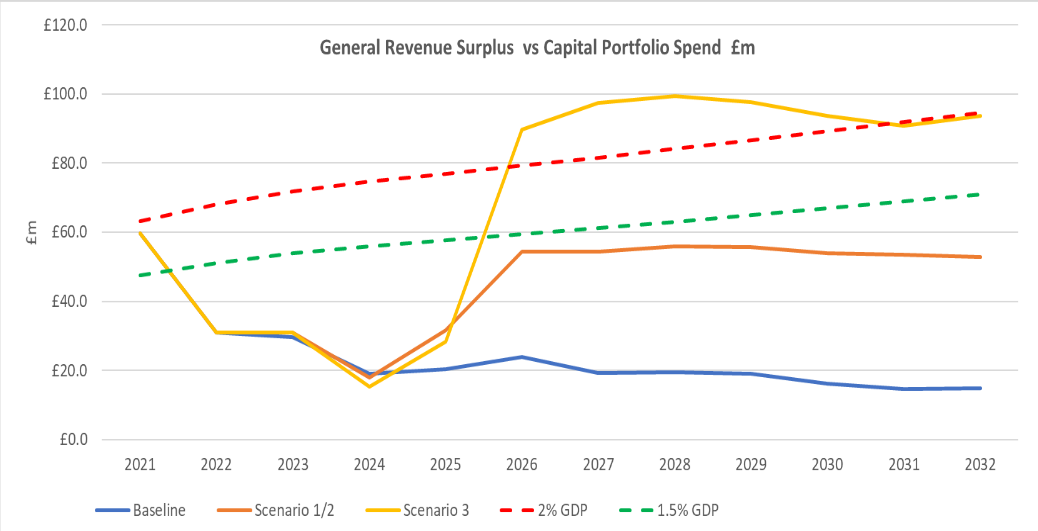


Figure 3

9.10 To achieve a long term sustainable financial position, the States need to have a revenue surplus higher than the required capital spend, regardless of whether it is funded through reserves or borrowing. In the chart above (Figure 3) the solid line (the revenue surplus) needs to be higher than, or equal to, the red dotted line (capital expenditure) to be in a sustainable position.

9.11 The baseline (which includes no additional tax measures or cost savings) shows an increasingly negative picture, with very small surpluses generated, nowhere near sufficient to cover the cost of investing in the current prioritised capital projects or be able to invest in future terms' capital requirements.

9.12 Scenarios 1 and 2 (excluding the tax package but including additional motoring related and corporate taxes plus cost savings) show an improved position with revenue surpluses expected to reach approximately £55m per annum. However, as the chart in Figure 3 highlights, these surpluses are not sufficient to cover capital expenditure requirements.

9.13 Scenario 3 (including the full progressive tax package plus additional motoring and corporate taxes and cost savings) results in a significantly improved financial performance bringing the States back to financial sustainability by 2026.

<u>Fiscal Policy and Long-Term Financial Sustainability</u>

9.14 The agreed Fiscal Policy Framework states:

"Principle 3: Guernsey's Fiscal Policy should operate on a principle of long-term permanent balance."

9.15 The analysis and chart in Figure 3 above show that Scenario 3 is the only sustainable option in the ten-year forecasting window that meets Principle 3.

9.16 Towards the end of the 10-year window the Scenario 3 revenue surplus levels off and is projected very slightly below the capital projection at 2% of GDP indicating that this may not be sustainable beyond the ten-year window modelled, however it should be noted that:

i. This reduction in General Revenue growth is owing to the level of General Revenue contributions (transferred as part of the Health Service Fund) being routed back into the contributory funds to make-up any lost income due to the implementation of the tax package. By 2032 this levels off as it comes into line with the previously approved ten-year increases to contributory rates.

ii. From 2035 the secondary pension impact starts to improve as pensions begin to be drawn and become taxable. Early in its implementation the States' financial performance is negatively impacted as taxable income reduces as pension contributions are not taxable. However, in the long-term secondary pensions should have an overall positive effect.

9.17 The improvement expected to result from secondary pensions compared to the estimated revenue impact assumed in 2032 is approximately £10m each year, however the realisation of these benefits is well outside the window of this F&I Plan given that modelling has indicated that the benefits will start to be realised in 50 – 60 years' time.

9.18 Even with these benefits included in the long-term forecast, Scenario 3 is the only option that results in long-term sustainability according to Principle 3 of the Fiscal Policy.

10. Total Funding Requirement – Overall Surplus Deficit

10.1 This section will discuss the total funding requirement for each scenario. It will bring together projections for General Revenue as shown in Figure 3 above, in addition to projections for the contributory funds plus estimated capital expenditure based on the selected portfolio for each scenario.

<u>Contributory Funds</u>

10.2 In October 2021, following consideration of the report entitled 'Contributory Benefits and Contributions rates for 2022[6]', the States approved plans to increase the percentage contribution rates to the Guernsey Insurance Fund (GIF)

[6] Billet d'État XX, 2021

over 10 years and the Long-term Care Insurance Fund (LTCIF) over four years. The States resolved:

> "To increase the percentage contribution rate for employers and employees into the Guernsey Insurance Fund in increments of 0.1% each per year over ten years, and for self-employed persons, and non-employed persons under pension age in increments of 0.2% per year over ten years, with effect from 1st January 2022, as set out in paragraph 3.11 of that Policy Letter".

and:

> "To increase the percentage contribution rate for employees, self-employed persons, and non-employed persons under and over pension age, into the Long-term Care Insurance Fund in increments of 0.1% per year over four years, with effect from 1 January 2022, as set out in paragraph 3.18 of that Policy Letter".

10.3 It should be noted that the increase to the Long-Term Care Insurance Fund of 0.4% was based on the current model of long-term care funding (i.e. excluding the provision of care at home). The actuarial review completed at the time highlighted that if the Long-term Care Insurance Scheme was extended to cover the provision of care delivered at home, the percentage contribution rates would need to increase by 1% to make the Long-term Care Insurance Fund sustainable in the long-term.

10.4 The first year's increase was applied in 2022, this being the first contribution rate increase since 2017 and the funds will have received increased contributions of approximately £10m for 2022-2023 raised from the increases in contribution rates already applied in 2022 and 2023.

10.5 The chart in Figure 4 below shows the projected revenue deficit excluding investment returns as well as the net surplus including investment returns. These projections include the ten-year increase to contribution rates. Excluding the investment returns the funds' deficit in latest forecasts equates to approximately £15m per annum. The funds therefore become financially sustainable when an investment return is made in excess of £15m.

10.6 The Guernsey Insurance Fund balance at the start of 2023 was £720m and the Long-term Care Fund balance was £129m. The investment returns on these reserves can therefore make a significant difference to the underlying result of the social security financial performance. The long-term rate assumed for estimating investment returns is a prudent 2.5% above inflation, equating to approximately £42m 2023.

10.7 Scenario 3 proposes a restructure to the social security contributions which addresses the inequities inherent in the current social security contributions system, therefore directly helping those on the lowest incomes and making the system more progressive. It has been assumed that any lost income to the funds will be offset by re-routing some of the General Revenue contributions (the Health Service contributions currently routed through to General Revenue) into the GIF/LTC, making up any shortfall. The projections are therefore the same in all scenarios.

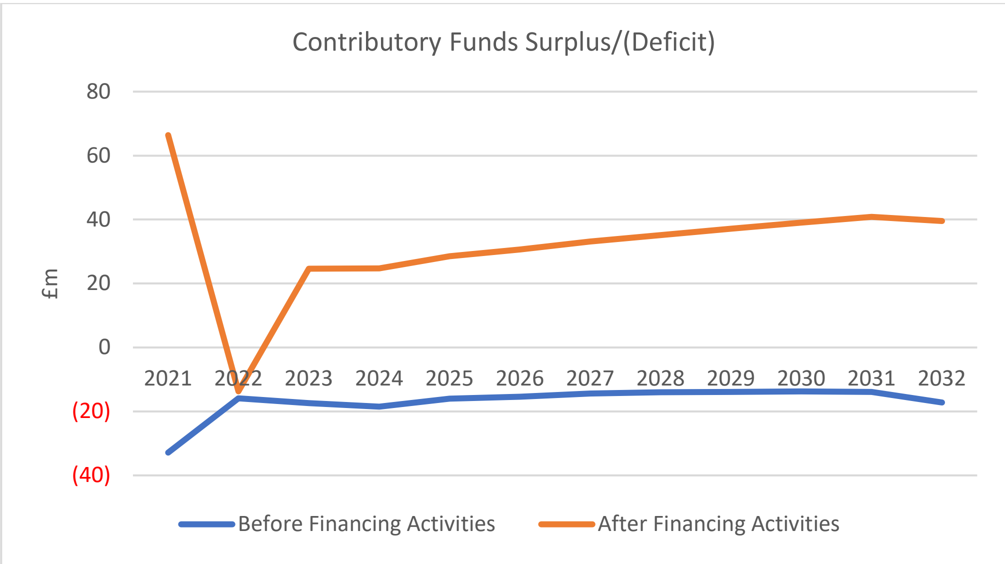


Figure 4

<u>Overall Funding Requirement</u>

10.8 The charts below show the overall funding requirement of the States after taking into account capital expenditure, the social security funds as described above and the net impact of any financing activities.

10.9 The chart in Figure 5 highlights the overall surplus / deficit for each scenario including financing activities. In 2026 all scenarios reflect an overall surplus, however whereas Scenario 3 continues in a strong position, Scenarios 1 and 2 show a decline to a very small surplus by 2032. This position is driven by an average £35m net surplus generated on the contributory funds from 2026 onwards once investment returns are included. Owing to the size of the contributory funds the investment returns make a significant difference to their financial performance.

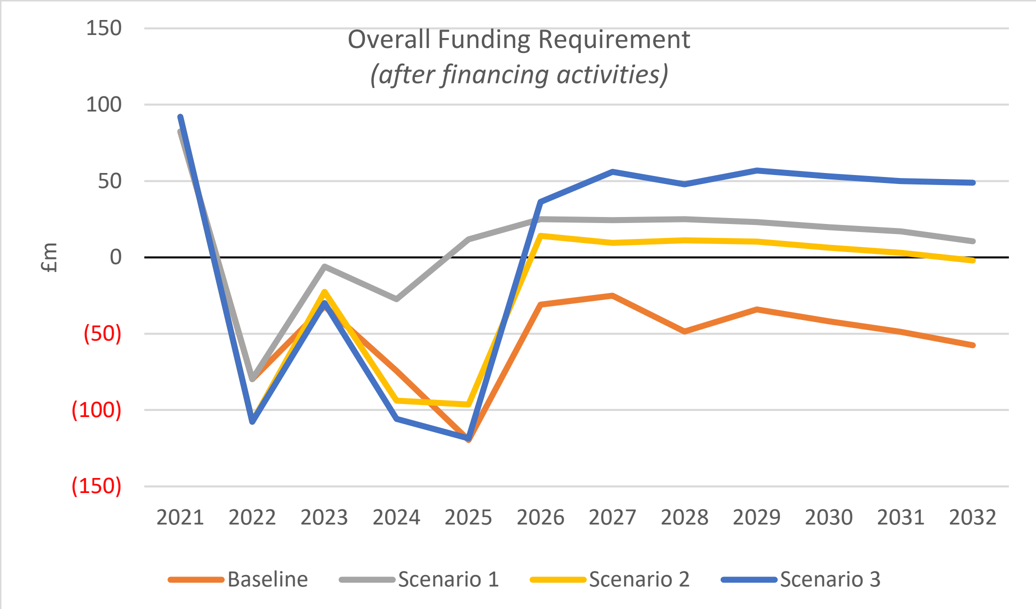


Figure 5

10.10 The chart in Figure 6 shows the same overall surplus / deficit for each scenario but this chart *excludes* the net impact from financing activities. This changes the trend significantly and shows the underlying funding requirements before financing activities and investment returns are taken into account.

10.11 When financing activities are excluded the overall deficit for both Scenarios 1 and 2 is forecast at approximately £60m per year by 2032, a position that is clearly not sustainable in the long term.

10.12 Scenario 3 also moves from an overall surplus to small overall deficit once the impact of financing activities is stripped out is due to the continued underlying deficit forecast (c£15m) on the social security funds. As indicated in section 9.16 this deficit would level out and start to improve with the realisation of benefits from secondary pensions and the stabilisation of the level of contributions transferred from General Revenue to the Contributory Funds.

10.13 The charts indicate that the underlying financial performance of the States is particularly sensitive to investment returns.

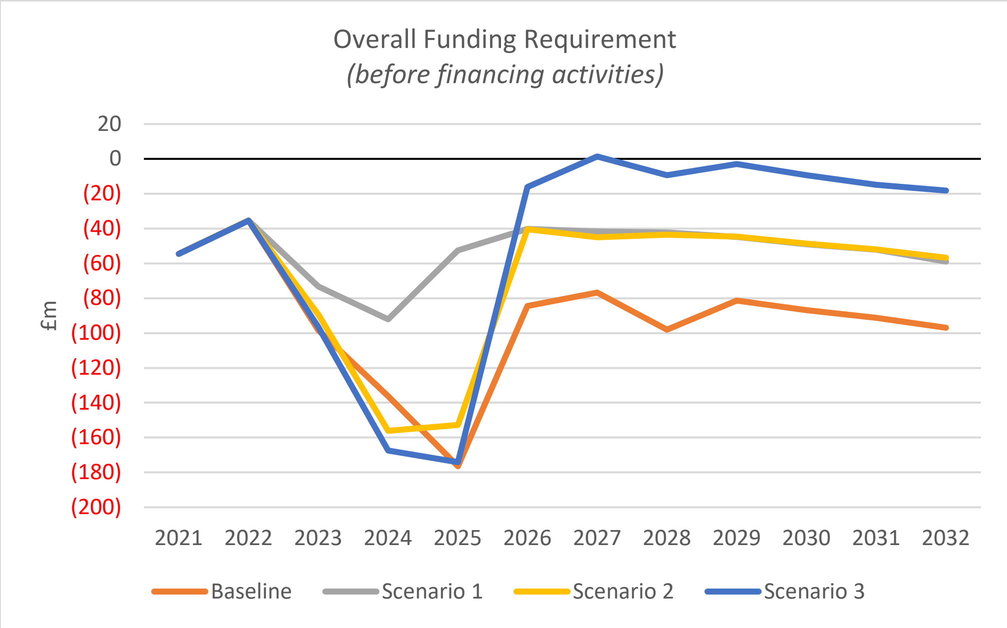


Figure 6

Structural Deficit

10.14 A structural deficit is defined as a government deficit that is independent of the business cycle and is created when a government is spending more than the long-term average tax revenues it is receiving.

10.15 While the charts above show the overall surplus / deficit, which is defined as revenue income less revenue expenditure and capital spend, they are not structural deficit charts owing to the high capital expenditure in the current political term, as well as cyclical revenue and cost trends that impact the financial position.

10.16 The key focus of the F&I Plan is on the funding and financing requirement of the States. However, the current structural deficit is explored in this section of the report for completeness and a high-level estimate of the structural deficit is illustrated in the following table.

Structural Deficit - £'000	**2022**
Overall Deficit as per 2022 Accounts	(134,822)
Less 2022 investment return/loss	93,878
Less 2022 cyclical income	(7,000)
Adjust depreciation & project spend	(18,760)
Structural Deficit excl. investment return	**(66,704)**

10.17 The above table indicates a structural deficit of circa £67m based on the 2022 Accounts. The accounting deficit has been adjusted as follows:

i) The unrealised investment loss of £94m for the year has been stripped out which is really capital appreciation/depreciation rather than income.

ii) Cyclical income has been reflected resulting in a £7m adjustment. This consists of an adjustment down for high levels of document duty driven by both volume and price increases. Company income tax has also been normalised due to high levels of activity in non-banking financial services.

iii) Finally, an adjustment has been put through to normalise the depreciation charge to what it would be if investment in capital expenditure had continued at a consistent level to compensate for under-investment over a number of years leading to lower depreciation charges (as discussed in paragraph 4.14). An adjustment has also been made to reflect project spend which has to be expensed in year.

10.18 The structural deficit is based on current revenues and services and does not take account of the future service demands, the ageing demographic or other cost pressures, which are all expected to worsen the position over the coming years.

10.19 The calculation excludes investment returns as these do not represent the underlying financial performance of the States and cannot be relied upon to fund service provision or priorities of the States.

10.20 It should be noted that projections beyond 2028 within this F&I Plan, where a standard assumption has been made for capital, and long-term assumptions have been applied to costs and revenues, do in fact illustrate the forecast structural deficit of the States of Guernsey.

11. Balancing the Books – Route to Sustainability

11.1 This section discusses ways in which the States could return to sustainable public finances.

Progressive Tax Package

11.2 In early 2023, the States considered a package of measures representing a significant restructure of the way in which Guernsey might raise revenues[7].

[7] Billet d'État III, 2023

11.3 The core package presented a reduction in income tax and social security contributions for most lower- and middle-income households. This included the addition of an allowance to the social security contributions, an increase in the personal income tax allowance and the introduction of a 15% tax band on income between the personal tax allowance and £30,000. At the core of this restructure was a broad-based Goods & Services Tax (GST) at 5%. The full details of the package proposed can be found in 'The Tax Review: Phase 2' policy letter[8].

11.4 This package is estimated to raise £59m, adjusted for inflation and earnings growth. Of this, £26m would be raised from corporate entities via increases in employer contributions and an International Services Entities Fee within the GST structure that captures a larger contribution from the finance sector. An estimated £26m will be raised from households. Most lower income households could expect to be better off, and most of the additional revenue would be derived from higher income households. £7m is expected to be generated from visitor spend.

11.5 Given the increasingly evident structural deficit and the challenges of funding the capital portfolio in the foreseeable future, the Committee has opted to present what the financial situation would look like if this package had been accepted and so have reflected this package into the financial projections in Scenario 3 alongside further revenue raising totalling £10m from a tax on vehicle ownership and £15m from the application of changes to corporate taxes and corporate levies.

11.6 Combined, this package would raise aggregate government revenues from around 21% of GDP to between 23% and 24% of GDP. This would place Guernsey on a more comparable footing with Jersey, which raises around 26% of GDP in revenues.

11.7 It would also broaden the tax base away from its current high concentration on taxes on income, providing greater resilience given the ageing demographic. Reviewing the experience in Jersey over the last decade, revenues from GST have typically moved quite differently to personal income tax revenues, with a weak year in one often coinciding with stronger growth in the other. Overall, the annual growth rate in GST over the last decade (during which time there has been no change in the rate) has averaged slightly higher (by about 0.24% a year) than the growth in personal income tax receipts, which is reflected in this Plan's forecasting.

[8] Billet d'État II, 2023

Zero-Rating Food

11.8 As part of the Tax Review debate there was much discussion about the application of GST to food. The Committee's preference is still to apply GST on as broad a base as possible, as critically it makes the administration of the GST simpler and less expensive to run.

11.9 For businesses, it means they have only a single rate to deal with and will not have to apply different treatments to different product lines. It is also likely to reduce compliance activity for businesses. For the Revenue Service, it reduces the likelihood of error in the submission of quarterly returns and minimises compliance activity. For the Guernsey Border Agency it reduces the complexity involved in determining whether imported goods are taxable, or, if they face a mixed delivery, how much of the value of the import is taxable and how much zero rated.

11.10 It is for these reasons that many jurisdictions including Jersey (2009), New Zealand (1986), Saudi Arabia (2018) and UAE (2018) have introduced broad-based and relatively low-rate schemes with only limited exemptions or zero-rating. All of these systems include a GST or similar tax on food.

11.11 While analysis shows that lower income households spend a higher proportion of their income on food than higher income households, in monetary terms higher income households spend significantly more on food. This means that the benefit of zero-rating food is poorly targeted and more of the lost revenue is to the benefit of households in the richest 30% than the poorest 30%.

11.12 Since the application of a zero rate to food would make a significant reduction in the revenue generated, it would be necessary to apply a higher rate to all other taxable goods and services in order to raise the same amount of revenue. In doing so almost all the benefit to lower income households is lost.

11.13 The figure below (Figure 7) shows a comparison of the package presented in the Tax Review at 5% including food (grey bars) and at 6% with a zero-rating of all food items (blue bars). This graph illustrates that as a percentage of household income excluding food would have the biggest impact on the poorest 5% of households. For these households excluding food and changing the rate to 6% would mean they pay more tax overall. Note that the example income levels of the chart are for the household, i.e. for both adults combined in a two adult household.

11.14 However, the Committee accepts that there is some preference within the Assembly to consider a GST without food and therefore presents the option of a GST at 6% with a zero-rating on all food and non-alcoholic drink products (for the sake of simplicity including those purchased in cafes or restaurants) as an alternative to the preferred scheme where the GST is applied at 5% including food.

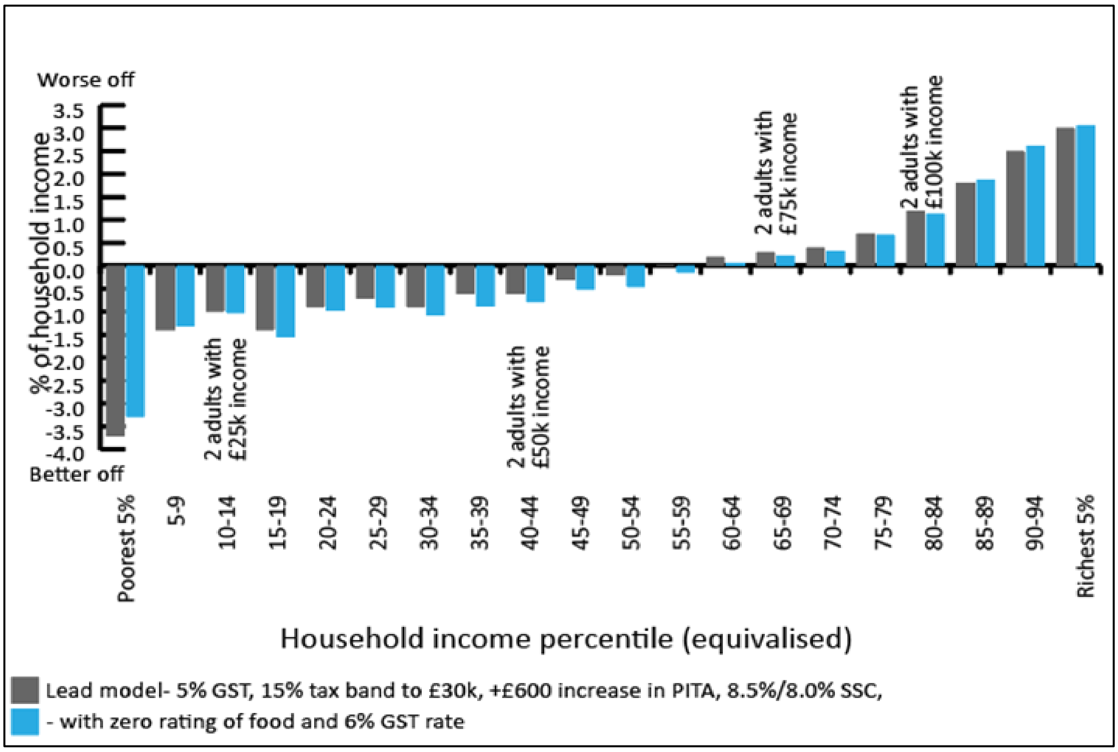


Figure 7

GST and the Restructure of Social Security Contributions

11.15 Within Scenario 3 it is proposed that the social security contributions system would be restructured in line with the proposals of the Tax Review. That includes the application of an allowance, matched to the personal income tax allowance, for all classes of contributors except employers (a facility only non-employed people and pensioners benefit from currently), and a change in the basis for assessment to all income for all contributors, meaning everyone is assessed on the same definition of income.

11.16 The restructure would also add a 2% rate for employer contributions above the upper earnings limit up to £250,000. To balance the income lost in the provision of allowances, the restructure would apply slightly higher rates than those applied under the ten-year phased increase in contributions agreed in 2021 (which was applied in 2022 and 2023 and is expected to continue in 2024). The net result would be to shift the burden of contribution revenues so that those on lower incomes pay less and those on higher incomes may pay more. This restructure raises around £16m less than the phased increase agreed in 2021, so Scenario 3 assumes that this will be made up by a reduction in the amount transferred from contributions to General Revenue.

11.17 Within Scenarios 1 and 2, it is assumed that the Social Security contribution rates continue to follow the phased increases agreed in 2021. This is modelled under the assumption that it operates under the current contributions structure, however, the Committee *for* Employment & Social Security has expressed a wish to pursue a restructure outside the context of any wider revenue raising should that be necessary.

11.18 The restructure would need to match the revenue raised by the phased increase in contribution rates agreed in 2021 if it is to retain the financial integrity of the Guernsey Insurance and Long-Term Care funds. Without any significant revenue raising from a GST or other tax this would likely mean that the allowance applied to contributions would need to be smaller than the personal income tax allowance, and may require slightly higher contribution rates, but could still result in a contribution system which is overall fairer and more progressive than that currently in place.

11.19 Scenarios 1 and 2 could therefore be considered as including either the continuation of the phased increase in contributions already begun, or a restructured contributions system raising an equivalent amount of money. It is anticipated that the Committee *for* Employment & Social Security would be likely to bring forward recommendations to develop the latter of these two options if the Assembly opt for either of Scenarios 1 or 2.

Income taxes

11.20 It has been suggested that simply taxing income would be fairer and easier. However, Guernsey already raises almost two thirds of its revenue from taxes charged against people's income. That makes the Government's revenues particularly exposed to risks relating to the number of people working in the community and how much they earn. Given the population is ageing, it is also necessary to consider that most people have less income in retirement than they had in their working lives, but they might have as much discretionary spending because their mortgage is paid or they have capital from savings, a lump sum pension pay-out or downsizing to support their lifestyle.

11.21 Guernsey's heavy reliance on income-based taxes increases vulnerability to labour market shocks. For example, between 2008 and 2010, at the height of the financial crisis, personal income tax receipts fell in real terms by 11% or £35m at today's prices. Over the same period social security contributions increased by only 1%. This is despite real increases of more than 20% to the upper earnings limit on employee and self-employed contributions during this period which should have resulted in a much larger increase in revenues (from £64,896 in 2008 to £79,872 in 2010). A similar effect was seen in 2020 when COVID-19 lockdowns reduced people's income, although the impact was softened by the payment of business support.

11.22 Having a variety of different revenue streams helps smooth these kinds of effects. While income and consumption are related, the analysis of revenues in Jersey suggests that the two income streams often react quite differently to economic changes, meaning that having both within the tax base adds a stability, resilience, and should smooth volatility in incomes.

11.23 In all the scenarios presented, some additional revenue raising is being achieved by charges on income, through the already agreed increases in the social security system. This reflects both the extent to which the pensions and long-term care schemes are a source of long-term spending pressures, and the greater tolerance within the community for increases in contributions.

11.24 The structure of the income tax system, and in particular the headline rate and the rate applied to higher earners, can impact Guernsey's competitive position and its ability to attract workers to the Island. Both the headline rate, and higher earners' rates are easily comparable when making competitive comparisons between jurisdictions, and Guernsey will be compared to both Jersey with their "20 means 20" headline application, and the Isle of man with a 10% "standard" rate and a 20% "higher" rate.

11.25 A 1% increase in the income tax rate would raise £16m at 2023 prices, so to close the gap of £40m-£60m in Scenario 2 a significant increase of between 2.5% and 4% would need to be added to the headline rate.

11.26 When considering a higher rate of tax for high earners, the marginal rate of tax for the additional income earned over the threshold should be considered. This is particularly important when the withdrawal of tax allowances for those with an income above £90,000 is also factored in. Ideally, the threshold for a higher rate would be set at or above the point at which an individual stops paying full rate Social Security Contributions to avoid creating a high marginal rate for those subject to both.

11.27 The high upper earnings limit applied to Social Security Contributions in Guernsey means that contributions are paid at full rate to a much higher level in Guernsey (£168,480) than in either Jersey or the Isle of Man (£60,720 and £44,928 respectively). This significantly limits the revenue raising potential of a higher earners rate, since very few people would be subject to it. Each 1% on income above the upper earnings limit would raise less than £2m and raise revenue from just 5% of households.

11.28 Given Guernsey's economic make-up, raising rates of income tax would not raise the levels of additional tax required while maintaining a competitive rate compared with other Jurisdictions. To raise any significant taxes would create competitive imbalance with competing jurisdictions, putting at risk the States' agreed policy on net migration and creating a potential economic risk. Applying a GST, however, would place Guernsey on a similar footing to the other crown dependencies.

Corporate Taxes

Review of Corporate Tax Options

11.29 As part of the Tax Review Phase 2, Ernst and Young (EY) was commissioned to review corporate tax options for Guernsey. In its report "Review of Corporate Tax options" dated 30 September 2022[9], different options for increasing corporate taxes were reviewed and their potential economic impact modelled taking into account economic behavioural changes (for example, companies relocating to another jurisdiction as a result of tax increases).

11.30 Four options were modelled:

Option 1	This option retains the existing 0/10/20 regime and increases the tax rate applied to domestic sectors and those which currently already pay Corporate Income Tax.
Option 2	Replacing the 0/10/20 structure with a single rate (15%) on all domestic active and passive income under a territorial regime. While this single rate increases the tax rate for most sectors, some sectors which are subject to a 20% tax rate under the current regime, would benefit from a tax reduction. Sectors that have been identified as "red line" are not taxed within this option.
Option 2a	This is a variation of Option 2 where no sector is "red line", and all sectors face Corporate Income Tax at a rate of 15% under the territorial regime.
Option 4	This option assumes a flat levy, rather than a profits-related tax rate. The option broadens the "tax" base and brings within charge those economic operators which do not currently contribute through the tax system. This would retain the "zero-tax" regime and, depending on how the levy is structured, could potentially be viewed as a cost of doing business in Guernsey rather than as a tax.

11.31 In all of the options modelled, the revenue raising/ tax increases were below £20m.

[9] Billet d'État III, 2023

Source: EY analysis

Option	Tax impact	GVA impact	
Option 1	£19.2m	(£40.1m)	(1.3%)
Option 2	£18.4m	(£34.3m)	(1.1%)
Option 2a	£9.1m	(£352.7m)	(11.1%)
Option 4	£16 – 20m		

Tax Sub Committee Update: Corporate Taxes

11.32 The Policy & Resources Committee through the Tax Sub-Committee is now progressing work on areas where more revenue might be raised from corporate entities, and this F&I Plan includes an assumption of £15m of additional revenue from this source as detailed below.

11.33 On 19 May 2023, the Treasury Lead jointly announced with his counterparts in Jersey and the Isle of Man, the intention to implement the OECD Pillar 2 initiative, which would provide for a 15% effective tax rate for large in-scope multinational enterprises (those with a global revenue of more than €750m), from 2025. The Tax Sub-Committee has established a potential minimum of £10m additional revenues from this change.

11.34 Ministerial engagement with Jersey and the Isle of Man suggests that if Guernsey were to seek to introduce further fundamental structural changes to the corporate tax regime (prior to the Pillar 2 proposals being embedded and their impact fully assessed) or make changes to the rate, it would not be doing so in a lock-step approach with the other islands. The proposals will impact most banking activity and a large proportion of insurance activity on the Island, overlapping considerably with the potential revenues identified by EY in either Option 1 or 2 of their 2022 report.

11.35 Given the competitive risk in Guernsey proceeding in isolation, prior to neighbouring jurisdictions, the Tax Sub-Committee is recommending no further substantive structural changes other than continuing to explore opportunities to expand the existing company intermediate 10% rate and company higher 20% rate.

11.36 A review is being undertaken to identify opportunities to extend these rates to other businesses, taking into consideration the effective tax rate of those sectors. Engagement with the sectors where the rate could potentially be increased is taking place and the feedback being considered.

11.37 The data is also being analysed to understand the proportion of companies that already regularly distribute their profits, as in these cases the net gain would be limited (i.e. it would be largely a timing difference of when tax is paid).

11.38 The Tax Sub-Committee's view is that the immediate opportunities for revenue raising from extensions to the 10% and 20% rate are limited.

11.39 A review is underway to establish the scale of accumulated, untaxed undistributed profits in Guernsey resident companies following which there will be consideration of policy options to address any identified issues. In the future it is planned that this information will be collected on tax returns to enable appropriate monitoring.

11.40 Consideration is being given by the Tax Sub-Committee to an increase in registry fees including annual validation and administrative fees.

11.41 The Tax Sub-Committee was provided with the direction by P&R: *"To explore an alternative corporate vehicle or other appropriate form of entity or taxing structure which will be subject to income tax at 15% or such other rate or basis as the review may determine."* There has been consultation with industry on this matter which has established limited industry appetite, with those that are interested already in scope of Pillar 2. The conclusion of the group was that this should not be pursued further.

11.42 Taxe d'Abonnement is also under consideration. This is a tax applied as a small percentage of fund assets on an annual basis, similar to the tax applied in Luxembourg. The tax has revenue raising potential but could also significantly impact the ability to attract new fund businesses which could make it unsustainable in the long term. A consultation will be launched on this matter shortly.

Other Revenue Raising Initiatives

11.43 The Policy & Resources Committee is also pursuing elements of vehicle ownership taxes and transport taxes in conjunction with the Committee *for the* Environment & Infrastructure and there is an additional allowance of £10m for such revenue raising in this area. It is hoped that further updates on this work will be available for the 2024 Budget.

11.44 Property taxes have been explored by the Tax Sub-Committee and an additional tax on property is not recommended. However, it is felt that there is still scope to increase domestic TRP and recommendations have been made to P&R on this subject. £1m of annual real terms revenue raising has been included in this F&I Plan.

Savings as a Route to Sustainability

11.45 Following the outcome of the Tax Review debate in February 2023, a sub-committee has been set up to explore potential cost savings. This committee will be reporting back to the States by Summer 2024 so that any proposals can be included in the 2025 Budget. The States resolved that P&R should (inter alia):

> *"Establish a Sub-Committee to identify and review essential community services and, working with all Principal Committees and wider States Members, consider where efficiencies, structural change, cessation, outsourcing, restricting access to and/or commissioning of those services could deliver significant savings, and to incorporate these into a medium-term plan for delivering overall cost reductions of at least £10-16m over five years to be considered by the States no later than July 2024 for incorporation into the States of Guernsey Annual Budget for 2025"*

11.46 The Cost Saving Sub-Committee is well under way in its work, and engagement with Committees is ongoing. Analysis of the c2,000 suggestions from public and staff surveys is being analysed and scored and the next step will be to discuss the ideas raised with the relevant Committees. Initial feedback is that there is plenty to look at but a lot of the ideas were around taxation or increasing/introducing other charges rather than cost savings.

11.47 This F&I Plan contains annual recurring savings in each scenario of up to £10m phased in over several years as shown below. This is considered a challenging but realistic target to deliver.

- 2024 - £2.5m
- 2025 - £4.0m
- 2026 - £5.5m
- 2027 - £7.0m
- 2028 - £8.5m
- 2029 – £10.0m

11.48 In Scenarios 1 and 2 the long term (after 2029) deficit is projected to be £40m-£60m per year as shown in Section 10 "Total Funding Requirement – Overall Surplus Deficit" (Figure 6). Without considerable changes to public services, it would be impossible to close this gap through savings, which would be in addition to the £10m already included.

11.49 A comparison of Guernsey's General Revenue and Social Security spend per capita shows that overall spend per capita in Guernsey is low (£12,300 per Capita) compared to other Jurisdictions. While individual categories are hard to compare, owing to potentially different categorisation, the overall total is inclusive of all costs and can be directly compared.

11.50 If Guernsey's ratio were the same as Jersey's at £13,100 per capita, the increase in spend would be over £50m per year, a 6% increase on current spend.

11.51 This highlights the challenges of delivering any significant savings in addition to the modelled £10m without significant reduction in public services compared to neighbouring jurisdictions.

Spend per Capita £	Guernsey (incl. Alderney, 2022)	Jersey (2022)	UK (2022-2023)
Population	65,747	103,267	67,220,000
Health, Social and Long-term Care	3,600	3,700	3,100
Pensions and benefits	3,800	3,500	4,800
Education	1,200	1,900	1,600
Other costs	3,700	4,000	4,100
Total Cost per Capita*	**12,300**	**13,100**	**13,600**

Figure 8

*excluding financing charges, defence cost, and non-cash costs

12. Funding for the Current Political Term

12.1 This section focuses on the current political term to ensure adequate liquidity for business-as-usual activities plus the prioritised capital portfolio. Whereas the longer-term view considers investment into capital expenditure at a flat rate of 2% per annum over an 8-year period, in reality the annual cashflows required by the prioritised projects within the portfolio vary considerably. It is therefore important to consider the short- and medium-term funding requirements within this Plan based on the prioritised capital portfolio spend forecasts.

<u>Capital Projects Overview</u>

12.2 Project or capital spend is categorised as either minor capital, capital portfolio or transformation. This spend is not included within Committee budgets.

12.3 Minor capital has a maximum limit of £2m per project and is for essential spend on buying or replacing operational assets. It is grouped into four main categories and each category has a 4-year funding allocation and is managed by an oversight board who have delegated authority to approve projects of up to £0.5m in value.

12.4 The four minor capital categories are:

i. Medical Equipment
ii. IT
iii. Vehicles & Other Equipment
iv. Property Maintenance & Minor Works

12.5 Transformation spend is for one-off initiatives that aim to reshape public services. These initiatives currently fall into Education, Sport & Culture, Health & Social Care and Corporate Services.

12.6 The capital portfolio funds larger projects or programmes with funding being prioritised over each political term. The current portfolio was prioritised at the start of the current political term. The estimated cost and phasing for each project has been provided by project leads.

<u>The 2021-2025 Prioritised portfolio</u>

12.7 The capital portfolio that had been prioritised from 2021-2025 was larger than usual. This was partly because of historic under investment in infrastructure assets.

12.8 The chart below (Figure 9) shows the level of investment in capital and transformation projects over the previous 10 years. While this varies significantly year to year, over 10 years the average is below 1.5% of GDP.

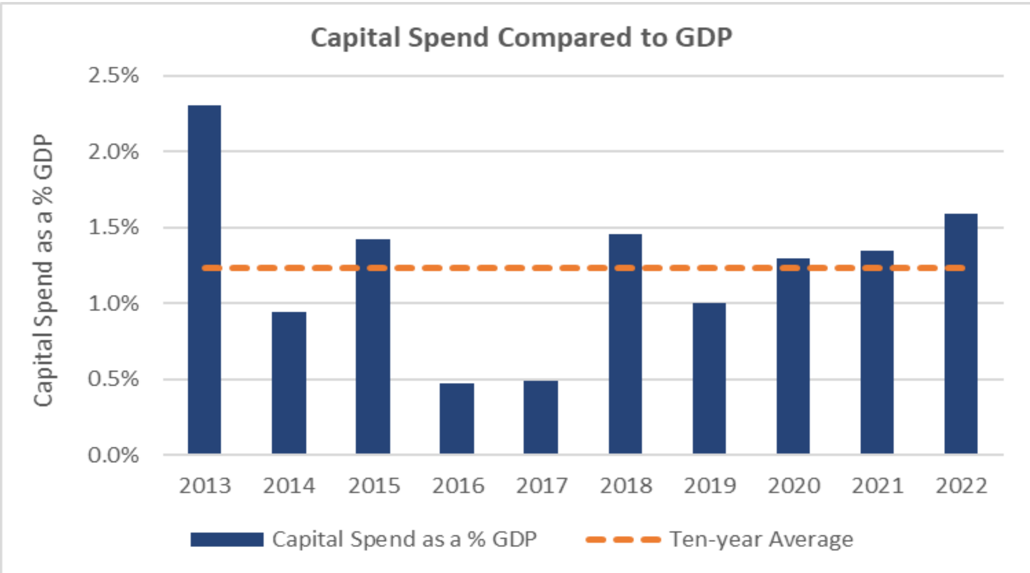


Figure 9

Review of the Capital Portfolio

12.9 A review of the capital portfolio was planned to take place during the term as the portfolio of projects matured. The full capital review report is attached in Annex 2.

12.10 There were concerns not only about affordability but also deliverability of the current portfolio, with both being key considerations in the review. The review included a number of engagement activities with both officers and Committees.

12.11 Post an initial review the Committee proposed a reduced portfolio recommending the re-categorisation of Our Hospital Modernisation Phase 2 project and associated works and the Future Inert Waste scheme as ‘pipeline’ rather than ‘delivery’, thereby significantly reducing the required investment levels in this political term and responding to both deliverability and affordability challenges. A review of the scope of several other projects was also suggested.

12.12 This initial proposal was then used as the basis for engagement with all committees to obtain political feedback as to the shape, content and size of the prioritised portfolio.

12.13 Through these political engagement sessions, the feedback received suggested the portfolio should increase in size and scope from what was being recommended to ensure appropriate investment was being made into critical government services. Generally, it was felt that the reduced portfolio put forward by the Committee did not meet the islands’ needs and that more investment was needed this term in services such as health, housing and waste management without de-prioritising other projects from the portfolio. It was this feedback that forms the basis for Scenario 3.

12.14 The table below (Figure 10) shows the cost of each capital portfolio as presented in the capital report in Annex 2. Portfolio 1 is significantly reduced driven by a substantial reduction in major capital compared to the other scenarios.

12.15 For all options the capital requirement for future political terms is assumed at 2% of GDP per annum.

Funding Required 2023-2025 £M	Current Portfolio	Portfolio 1	Portfolio 2	Portfolio 3
Major Capital	469	189	427	487
Minor Capital	62	64	62	62
Urgent & Unplanned	31	-	13	34
Transformation	25	13	25	25
Total Capital & One-Off	**587**	**266**	**527**	**608**
% GDP	**3.8%**	**2.2%**	**3.8%**	**4.1%**

Figure 10

12.16 Information provided by project teams indicates that significant investment is required in each capital portfolio option between 2023 and 2025, driven by large projects running concurrently as a result of underinvestment in previous years. This is then projected to return to 2% of GDP for all options. The chart below (Figure 11) shows the estimated phased cashflow requirements of each option as forecast by the project teams.

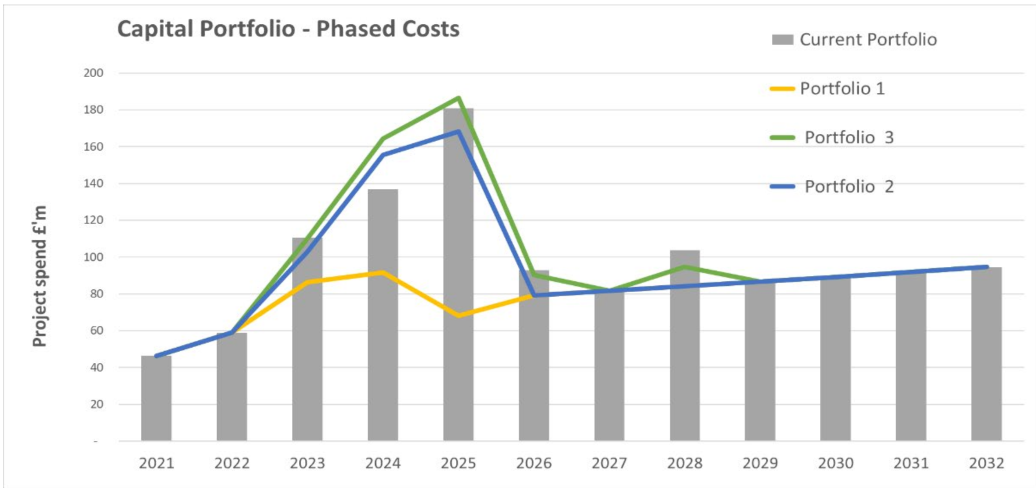


Figure 11

13. Current Reserves and Funding Requirement

13.1 The following section provides a summary of the States' cash reserves including the balance at the start of 2023 and describes what the reserves can be used for.

General Revenue Reserve

13.2 The General Revenue Reserve balance was £348m at 1 January 2023. This reserve is used to fund all of the States' General Revenue expenditure, including all capital, transformational and GWP initiatives. Its balance at the start of 2023 equates to approximately 59% of General Revenue income and to approximately 48% of the current prioritised capital portfolio including minor and transformation (baseline scenario) for this political term.

Guernsey Health Reserve (GHR)

13.3 In June 2019[10], the States considered the Policy & Resources Committee's policy letter entitled "Reform of Health Care Funding" and agreed the proposals to bring the governance of all health services provision unambiguously under the mandate of the Committee for Health & Social Care, the intention being to make the provision and funding of health services more transparent, effective and efficient.

13.4 The services previously funded from the Guernsey Health Service Fund (GHSF) were subsequently transferred to and managed through the budget of the Committee *for* Health & Social Care in 2022.

13.5 The revenues to fund these services are collected via the Social Security contributions system, but, with effect from 2022, the contributions previously to the Guernsey Health Service Fund were credited to General Revenue.

13.6 The GHSF was ring fenced and retained within the General Revenue Reserve as the Guernsey Health Reserve (GHR) from 1 January 2022. The balance of the GHR as at 1 January 2023 was £112m.

13.7 This Reserve can only be used to fund expenditure that meets the following criteria:

i. Unanticipated expenditure pressures in providing health services that arise outside of the normal budgetary process and cannot be met within that year's budget of the Committee for Health & Social Care;

ii. Revenue or capital expenditure on health transformation projects aimed at improving the efficiency, quality or capacity of health services in Guernsey which demonstrate long term benefits to the sustainability of Guernsey's health care system, subject to the same application process and governance conditions pertaining to the capital portfolio;

[10] Billet d'État X, 2019

iii. Any transitionary costs associated with implementing health related transformational programmes; and

iv. Revenue or capital expenditure on management of cost pressures developing within the health service provision over the long term associated with the ageing of the population.

13.8 Currently the GHR is used to fund the annual cost of NICE TAs (as directed by the States as the scheme was not affordable from ongoing revenues) as well as initiatives to reduce hospital waitlist and backlogs. Depending on the other uses of the health reserve, it is estimated that the GHR would be able to fund such costs for approximately 17-20 years.

13.9 The reserve could be considered to part-fund the OHM programme, however, with a balance of £112m at the end of 2022 it is not sufficient to fund the whole of OHM phase 2. In addition, doing so creates a further budget pressure as the NICE TAs and any other health initiatives would put further pressure on the baseline revenue position.

13.10 In Scenario 2 it has been assumed that NICE TA's are funded from General Revenue from 2025, creating a potential long-term revenue pressure in this option.

<u>States of Guernsey Bond</u>

13.11 The existing bond was issued in December 2014 and has a 32-year life, repayable in 2046. The States approved borrowing of up to £330m in 2014 with internal restrictions that it be used exclusively to lend on the capital to States-owned entities; trading accounts and funds; the Guernsey Housing Association; the Alderney Housing Association; and the Ladies' College. The terms of such loans were to be determined by the then Treasury & Resources Department but on the clear condition that repayments had to be made, in full, from a secure income stream and without direct recourse to General Revenue.

13.12 As at 1 January 2023, loans agreed from the proceeds amounted to £191m of which £140m remained outstanding. In the 2021 F&I Plan it was agreed that £160m of funds would be made available to fund the shortfall identified, and this remains available for use.

13.13 These funds (£160m) have since been allocated to the General Revenue Reserve and have brought that balance up to £508m on 1 January 2023. This equates to approximately 86% of General Revenue income (not including Committee income) and 78% of the capital and transformation costs prioritised for this term (baseline).

Core Investment Reserve

13.14 The Core Investment Reserve is the only long-term reserve, and the capital value is only available to be used in the exceptional and specific circumstances of severe and structural decline or major emergencies. In 2020, £50m was transferred from the Core Investment Reserve to the General Revenue Reserve to part-fund the impact of the COVID-19.

13.15 The States have a policy for the target balance of the Core Investment Reserve to equate to 100% of General Revenue Income in order to provide sufficient protection. The balance of the Core Investment Reserve at the end of 2022 was £158.1million which represents 26.4% of the 2022 General Revenue Income Budget. An amount of approximately £440m would need to be added to this Reserve to attain the target balance but appropriations can only be made if the budget moves back into an overall surplus position.

Funding requirement – the remaining political term

13.16 The cost of the portfolio over the next five years for Portfolios 1-3 is shown against the available funds in the table below (Figure 12).

13.17 All three scenarios retain the full balance of the General Revenue to ensure there are sufficient cash balances held in reserve for the next political term or for any unforeseen event, such as another pandemic.

13.18 The Guernsey Health Reserve, as highlighted previously, can only be used to fund specific expenditure. For Scenarios 1 and 3 the financial modelling supporting the F&I Plan assumes that it will be used to fund the approved NICE TAs and specific health GWP initiatives totalling £26m across the remainder of this term to 2025. For Scenario 2, it is assumed that the cost of NICE TAs is funded from the Unallocated General Reserve from 2025, and that the Health Service Reserve is used to part-fund the Hospital Modernisation Project. Depending on the timing of the project cashflow this could increase the use of the Health Service Reserve to up to £94m in this political term.

13.19 Further, it is assumed that the £160m unallocated balance of the bond is available to use for projects normally funded through the General Revenue reserve, as was agreed in the 2021 F&I Plan.

13.20 The projected cash surplus takes into account the General Revenue surplus of each Scenario generated over the remainder of this political term.

13.21 The table in Figure 12 highlights available funds for investment in capital expenditure over the remainder of this political term in each scenario. Scenario 3 is estimated to result in approximately £611m of available funds, Scenario 2 results in £535m of available funds and Scenario 1 is significantly reduced at £267m due to no additional borrowing. It should be noted that this excludes estimated investment returns on the balance of cash reserves.

13.22 The surplus for Scenario 3 is £6m lower than Scenarios 1 and 2 due to £5m being ringfenced for social and community initiatives. A further £1m cost is because of the revenue impact of the increased capital portfolio.

Existing Reserves/Bond £m	Balance	Available to Use			
	31.12.22	Baseline	Scenario 1	Scenario 2	Scenario 3
General Revenue Reserve	348	-	-	-	-
Bond	160	160	160	160	160
Health Service Reserve	112	26	26	94	26
Revenue Surplus (2023-25)[1]	-	69	81	81	75
New Borrowing		-	-	200	350
Available Reserves	**620**	**255**	**267**	**535**	**611**

Capital Funds Required This Term[2]	**Total Capex**	**588**	**266**	**526**	**608**
	Baseline	588			
	Portfolio 1		266		
	Portfolio 2			526	
	Portfolio 3				608

1. *Excludes investment return*
2. *Includes major, minor & transformation*

Figure 12

13.23 This demonstrates the large reduction in the size of the capital spend that would be required in Scenario 1, with no new borrowing. Capital spend would need to be limited to under half the cost of the current portfolio.

13.24 Scenario 2 illustrates that with borrowing and the use of the Health Service Reserve to part-fund OHM Phase 2 project, a larger capital portfolio can be afforded. However, this is still a reduction compared to the current portfolio meaning some projects would need to be paused or stopped altogether and others would require a significant review of scope.

13.25 Only in Scenario 3, with significant additional revenue raising measures combined with new borrowings, are all of the priorities put forward by Government affordable.

14. Long Term Analysis for Each Scenario

14.1 For each scenario the projections have been extended to 10 years and include the associated estimated reserves balance. While the three scenarios all ensure that General Revenue reserves (excluding the available bond) are retained at current levels to the end of this political term, it is important to understand how each scenario will affect the reserves in the future. This is to ensure that the future priorities of government can be afforded and ideally to ensure that the States have a plan to build reserves for the future to avoid the need for further borrowing.

14.2 The charts below show the projected net surplus *before* financing activities for Scenarios 1-3 (yellow line) and the phased capital investment requirement for the capital portfolio (red line), against the resulting reserves balance (grey bars). As soon as the yellow line (net surplus) is equal to or above the red line (capital spend) the financial position is stable.

14.3 In addition, the charts show a dotted black line indicating how current reserves (closing balance at end 2022) would grow if they were to increase in line with GDP growth.

Scenario 1

14.4 The chart in Figure 13 shows that the revenue surplus (yellow line) remains below the projected capital and transformation spend (red line) so this scenario is not financially sustainable.

14.5 The capital and transformation spend for this option is lower in this political term (the peak in 2023 – 2025 is lower) but the long term 2% GDP capital projection is the same in each scenario.

14.6 As a result, the reserves reduce to £333m including investment returns by 2032 (c£200m with investment return projected at inflation plus GDP growth). While reserves remain at an acceptable level in the ten-year timeframe, there is a significant and growing gap between the reserves forecast and where reserves should be if growing in line with GDP and this trend would be set to continue.

14.7 Scenario 1 only delays the decision for the States to agree a plan to financial sustainability to early in the next term. This scenario is only affordable in the short-term.

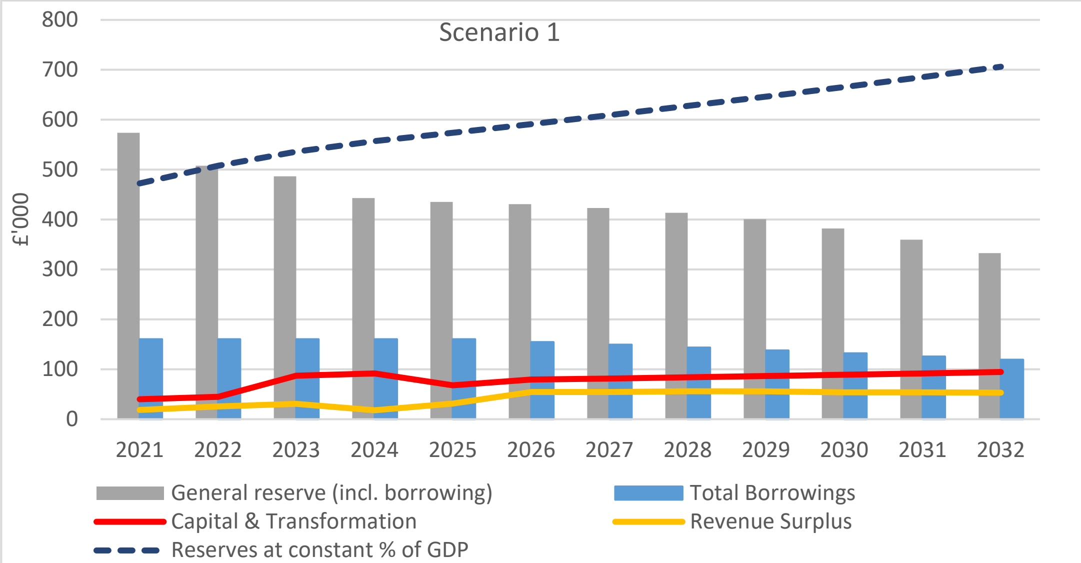


Figure 13

Scenario 2

14.8 The chart in figure 14 shows that the revenue surplus (yellow line) remains below the projected capital and transformation spend (red line) so this scenario is not financially sustainable.

14.9 The capital and transformation spend for this option is higher in this political term than in Scenario 1 due to higher capital spend funded by borrowing.

14.10 As a result, the reserves reduce to £277m including investment returns by 2032 (c£160m excluding projected investment returns). While reserves remain at an acceptable level in the short to medium term, there is a significant and growing gap between the reserves forecast and where reserves would be if growing in line with GDP.

14.11 In this scenario by the end of 2032 there would be no funds remaining in the Health Service Reserve (in the other scenarios there is an estimated £35m remaining in the Health Service Reserve at the end of 2032).

14.12 Whilst this scenario allows for greater capital investment this political term, the impact on reserves is greater because of the following:

a) The health reserve would no longer be funding the NICE TAs from 2025 placing additional funding pressure on General Revenue.
b) The new borrowing is projected to cost c £10m per year in interest with capital repayments of c£3.5m in 2032.

14.13 If the States were to choose Scenario 2 the decision regarding the long-term financial position becomes even more pressing.

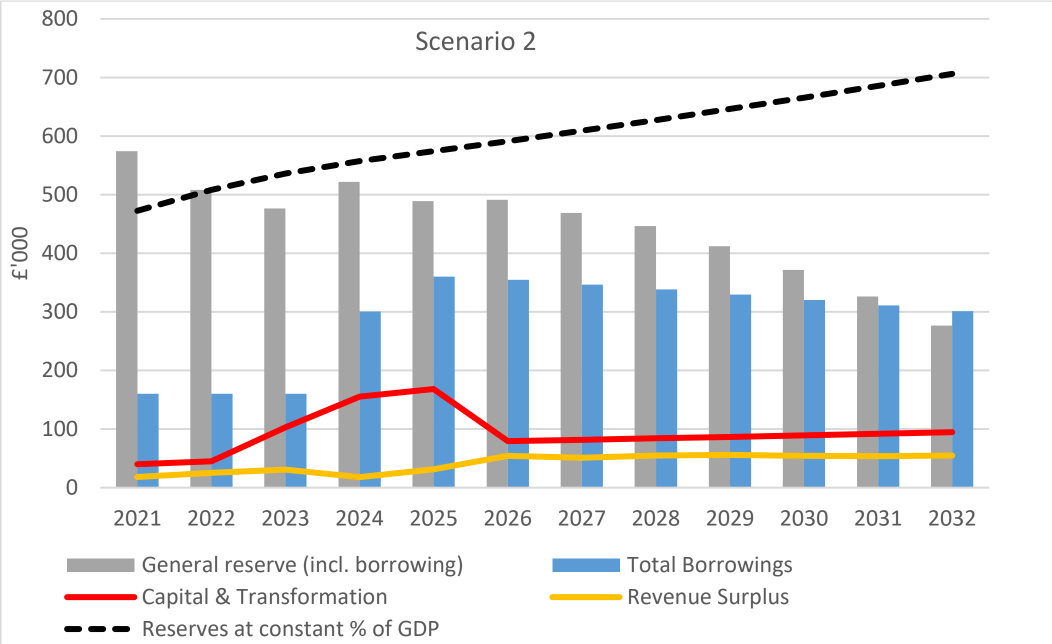


Figure 14

<u>Scenario 3</u>

14.14 The chart in figure 15 shows that the revenue surplus (yellow line) is above or in line with the projected capital and transformation spend (red line) so this Scenario is financially sustainable.

14.15 The capital and transformation spend peaks in 2025 before reducing to the equivalent of 2% of GDP.

14.16 The reserves balance is projected to increase from 2026 to 2030 due to the implementation of the progressive tax package. The additional revenue surplus is sufficient to service and repay the debt and to increase reserves. However, even in this Scenario there remains a gap between the reserves forecast and where they would be if growing in line with GDP.

14.17 By the end of 2032 there would be an estimated £35m remaining in the Health Service Reserve.

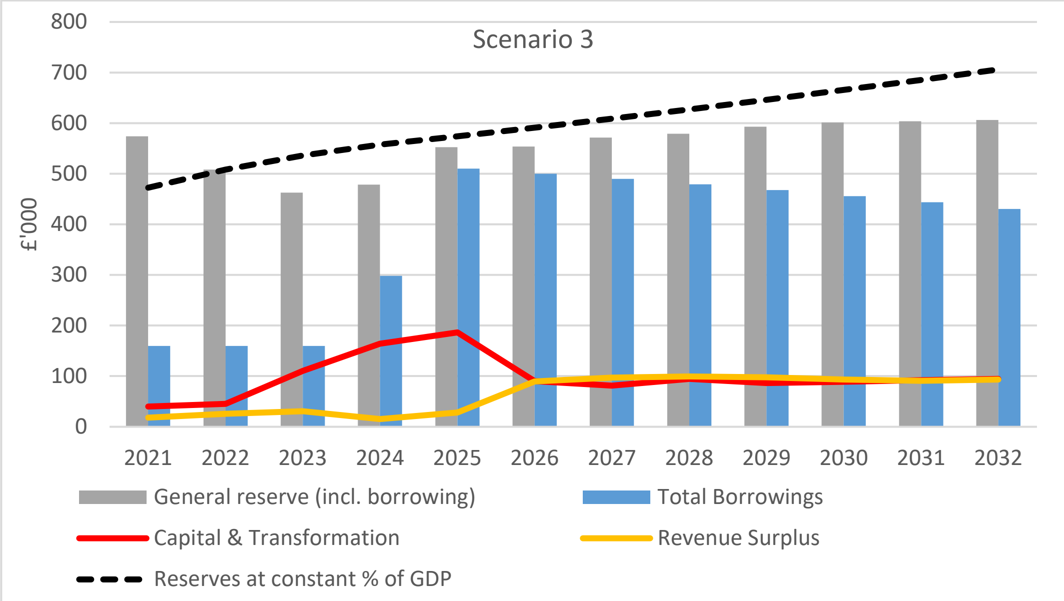


Figure 15

14.18 Clearly the only Scenario that returns the States to a position of long-term permanent balance and meets the requirements of Fiscal Policy Framework Rule 3 is Scenario 3.

15. Funding and Financing

15.1 To date, the States of Guernsey have operated a "save to spend" policy whereby projects are funded through historical surpluses. With depleting reserves and significant capital expenditure due to past under investment, this is no longer a sustainable position and both Scenarios 2 and 3 include borrowing to enable the progression of their associated capital portfolios.

15.2 Scenario 1 indicates the level of reduction that would need to be made to the current capital portfolio if the States do not approve any additional borrowing.

15.3 One of the main factors that led to Guernsey's recent credit rating downgrade was a decrease in liquid assets with no agreed plan to a way back to a sustainable financial position in the medium to long-term.

15.4 Prior to 2022 Guernsey received a one notch uplift to its credit rating owing to a very strong liquid asset reserve, which exceeded 100% of GDP. However, by the end of 2022 investment assets reduced to 85% of GDP and, combined with the failure to agree a tax package in early 2023 that would lead to financial stability, S&P dropped Guernsey's rating from AA- to A+.

15.5 With this in mind, the States now need to ensure that reserves are protected to ensure financial stability and to guard against further rating downgrades.

15.6 However, borrowing to fund prioritised services and projects that do not generate an income stream is a short-term solution only. The States will need to ensure they plan to return to a sustainable financial position to be able to pay back any borrowing and, importantly, start to build up reserves once again to meet the future investment needs of the Island.

15.7 Borrowing to fund the remaining capital portfolio prioritised this term will enable critical cash reserves to be maintained, which is not only prudent in cashflow planning, but will also enable the implementation of a longer-term investment strategy, which should yield better financial returns.

15.8 To protect the States' cash reserves and to ensure adequate liquidity to meet both planned and potentially unforeseen requirements it is therefore recommended that the States borrow to fund the capital portfolio.

15.9 In addition, it is critical the States agree a clear path to improving the net revenue position to ensure the ability to pay back any new debt and to be able to invest in future capital requirements, otherwise they will be creating a bigger problem for future Assemblies.

Borrowing in the last F&I Plan update

15.10 In the 2022 F&I Plan update it was calculated that no new borrowing was required to deliver the Plan. The policy letter stated:

"A Resolution from the debate on the GWP in 2021 allows the Policy & Resources Committee to enter into new external borrowing facilities up to a total maximum of £200m. According to the latest update, it is not anticipated that such borrowing will now be required. However, due to the continued uncertain economic conditions, the Committee does not wish to ask at this stage that the Resolution is rescinded. When the F&I Plan is reviewed in 2023, the forecast will be re-evaluated again. If it is still estimated that no new long-term borrowing will be required, the Committee will ask the Assembly to rescind that Resolution".

15.11 Although it looked as though no new borrowing was required 12 months ago, because of the changing financial position it appears that the States now need to borrow. The Resolution therefore will not be recommended for rescission.

15.12 There are a combination of factors informing this view. First, and most importantly, is the outcome of the Tax Review. The 2021 F&I Plan update fully projected reserves to be depleted after delivering the F&I Plan, however, it was considered likely at the time that there would be additional tax revenue streams that would enable reserves to be reinstated allowing for future capital plans to be afforded or future borrowing to be afforded.

15.13 As the Tax Review did not reach any conclusion on definitive and robust tax raising measures, it is now necessary to raise borrowing before reserves are depleted as low cash reserves would impact the States ability to borrow on the most favourable terms.

15.14 Second is the impact of the increasing cost of the capital portfolio. Over the last 12 months there have been significant inflationary factors particularly in the construction industry and estimates for some of the major programmes have increased correspondingly.

Current Borrowing Arrangements

15.15 The States of Guernsey bond was issued for £330m in 2014 for a period of 32 years, meaning that this will need to be repaid in 2046.

15.16 £190m of the bond has been loaned to projects that have a dedicated income stream and will repay the capital plus interest over the life of the project. Funds of £160m are still available for General Revenue and this is currently invested and earning interest as part of the investment portfolio.

15.17 Since the Bond was issued to the end of 2022 the investment return of the available funds within the Bond Reserve outperformed the coupon rate by an average of 1.7%. The poor general conditions and return for 2022 resulted in an average under-performance of 4.6% for the last two years (since the start of this F&I Plan), compared to an average out-performance of 4.1% to the end of 2021.

15.18 It was agreed in the 2021 F&I Plan debate that the balance of the bond proceeds, approximately £160m, be used to help fund the capital portfolio. Repayment of the capital element of this bond loan was not planned for the initial five-year period of the F&I Plan. It was assumed only interest was to be paid during this time.

15.19 The States also have access to a £100m revolving credit facility, which is used for short-term liquidity needs to avoid having to make a rushed withdrawal of investments.

15.20 While considering debt levels it should be noted that the Fiscal Framework states that total government debt should not exceed 15% of GDP. It goes on to say that gross debt can be accumulated only to fund capital investment with an identified revenue stream and that the maximum additional borrowing in any one States' term may not exceed the level of capital expenditure over that time period.

15.21 Currently the States have a debt-to-GDP ratio of approximately 9.5%, which is considerably less than other similar jurisdictions. For instance, Jersey, which has a credit rating of AA- (one notch above Guernsey) has an estimated debt/GDP ratio of 15.9% and is expected to grow to more than 22% based on current known plans. Bermuda, which has the same credit rating as Guernsey, has an estimated debt-to-GDP of 41.5% and Malta which is one notch below at A- has around 58.5% debt-to-GDP ratio. This suggests that Guernsey has comfortable headroom to incur further debt from a credit rating perspective.

New Borrowing - Scenario 1

15.22 As detailed earlier, there are no new borrowings assumed in Scenario 1 and as a result the capital portfolio would have to be significantly reduced to remain affordable.

New Borrowing -Scenario 2

15.23 Scenario 2 provides the States with a plan that is affordable in the short-to-medium-term as it assumes £200m of new borrowing in order to fund a larger capital portfolio for the current political term.

15.24 However, it does not fully stabilise the financial position or address the long-term deficit. The return to financial sustainability would still need to be firmly addressed over the next couple of years as described in the section "Long Term Analysis for Each Scenario". This Scenario creates an urgent requirement to reconsider long term financial sustainability early in the next political term.

15.25 While this Scenario protects cash reserves in the short term, the States would have committed to borrowing with no sustainable way to repay it in the long term.

15.26 It should be noted that taking out an additional £200m of debt falls under the 15% of GDP level as per the Fiscal Framework.

New Borrowing- Scenario 3

15.27 Scenario 3 presents a pathway to achieve financial sustainability, however, to protect reserves and afford the priorities of this political term during the implementation phase of the tax package, it recommends additional new borrowing of £350m.

15.28 Without any new borrowing, owing to the timing of the projected capital portfolio cashflows compared to the implementation of the new revenue generation measures, it would be necessary to draw on limited cash reserves to fund the proposed level of capital expenditure.

15.29 If the capital portfolio for this term is funded through reserves rather than debt, reserves are estimated to drop as low as £200m by 2025, which would not only put stress on States liquidity but could potentially risk a further ratings downgrade from S&P.

15.30 By taking out new borrowings, cash reserves would be maintained over the next few years when significant capital expenditure would be planned. As described in the section "Long Term Analysis for Each Scenario" the repayment of the debt (assumed repaid over 30 years) is affordable from the cash surpluses generated in this Scenario, as well as providing sufficient surpluses for investment in future capital expenditure.

15.31 Based on the cashflow projections it is therefore recommended that £350m of new debt is taken out to fund the future capital portfolio cash requirement. This level of debt would take the States up to approximately 18% of GDP by the end of 2026 based on latest GDP projections, which marginally and temporarily breaches the current Fiscal Policy Framework.

<u>Proposed Borrowing Structure</u>

15.32 Flexibility is important when considering the best type of debt facility, when timing and value of cashflows are uncertain, to ensure new debt is only incurred when required to avoid unnecessary costs. It was determined that the key factors the States should consider when assessing the use and type of debt to fund the capital portfolio requirement include:

i. <u>Minimise Funding Costs:</u> capital spend is forecast over a number of years, so it is important that new debt is only entered into when it is required. This will minimise costs, and risk, on unutilised debt funding over an extended period. Estimating the cashflow requirements of the capital portfolio has historically been challenging, which further increases the importance of the flexibility requirement.

ii. <u>Funding Security</u>: to reduce market risk exposure for future cashflows and to minimise risk that funding is not available on acceptable terms or pricing when required.

iii. <u>Preserve or Improve credit rating:</u> to ensure that an appropriate level of cash reserves is protected, and that any debt facility will help minimise against further downgrades.

15.33 Due to the difficulty in accurately estimating the timing of the projected cashflows of the capital portfolio and acknowledging that projections will change and become more accurate as projects mature and progress through the planning and implementation phases of the project lifecycle, a bridge-to-bond structure is recommended.

15.34 A bridge-to-bond is effectively where a bank facility, such as a Revolving Credit Facility, is utilised to fund cashflows until the facility reaches a certain size. When appropriate and once debt reaches a certain level, the bank facility can be converted into a public bond. This financing strategy is thought to best meet the objectives of flexibility, while minimising funding costs and attaining funding security.

15.35 A bond is considered the most cost-effective way of raising external debt and is available over longer tenures ranging from 10 to 50 years. However, the minimum amount a bond should be considered for is £250m as anything less would attract an illiquidity premium.

15.36 As the funding requirements of the capital portfolio are phased over a number of years it is not advised that a bond is taken out until the cashflows have been incurred or are highly likely to incur imminently, otherwise the States will be paying for a debt facility they are not using, which would not be cost effective.

15.37 Timing of debt issuance is key to minimise costs while balancing the need of funding security.

15.38 It is therefore recommended that a short-term bank facility is arranged, which can be drawn down when required to fund the capital portfolio cashflows. Once debt levels reach a certain amount (£250m+) this debt could be converted into a public bond at a time when market conditions are conducive for issuance. For Scenario 3 this would mean that a further £150m to £200m bank facility (depending on cashflow timings and long-term debt conversion) would be required in addition to the existing £100m Revolving Credit Facility.

15.39 For smaller issuances from £50m and upwards a US or UK private placement could be considered. This is similar to a bond although may have more restrictions and would be more costly than a bond. If Scenario 2 was agreed by the States then a more detailed analysis of the risk and benefits of a public bond versus a private placement would need to first be undertaken.

15.40 In addition to the key funding objectives of cost, flexibility and funding security, consideration should be given to environmental, social and governance (ESG) factors when determining the most suitable long-term debt financing facility. This could be in the form of ‘green’ bonds where the money raised targets environmentally friendly projects such as renewable energy, or perhaps a better suited ‘social’ bond where the focus is on projects with positive social outcomes, such as improving health or providing affordable housing. A social bond is also likely to come with better rates, linking into the key objective of minimising borrowing costs.

Additional Borrowing Requirements

15.41 In addition to the funding of the capital portfolio the Guernsey Housing Association (GHA) may also require additional long-term funding to enable it to finance the development of the States’ Affordable Housing Programme. Although the exact level of funding required is not yet known, an indicative amount of £100m has been assumed for planning purposes.

15.42 Should the States take out this debt on behalf of the GHA, this would increase debt-to-GDP levels to approximately 20% for Scenario 3 and 16% for Scenario 2. This debt will, however, come with a direct income stream that would repay both the interest expense and the principal sum, without putting additional expense on the States’ underlying financial performance. Gross debt levels would remain well within the current credit rating headroom, assuming liquidity remains strong. However, consideration would need to be given to the Fiscal Framework as including this debt on the States’ balance sheet would breach the 15% of GDP limit.

15.43 In addition, the Electricity Strategy, which is due to be debated on the 6 September 2023, asks the States to give direction and focus to the further work that needs to be done to develop the electricity strategy.

15.44 This is likely to include significant spend on electricity assets including renewable energy (range of £380m-£640m of capital funding required depending on the preferred option or “Supply Pathway”). It is unknown at present how any investment in infrastructure would be financed, however there is the possibility that at least some of the financing required would need to be guaranteed or underwritten by the States of Guernsey given the likely requirement to retain control of strategic assets for security of electricity supply provision.

15.45 This is not a given however and an outsourced model could be agreed for at least some elements of the capital investment, with the States of Guernsey passing all of the investment requirement, ownership and building (as well as operation and maintenance) to a third party.

15.46 It is unknown at this stage the size of the Electricity Strategy capital investment that the States would need to fund or guarantee borrowing for. If this was £400m, this would increase the total debt to 30% GDP for Scenario 3 and 26% GDP for Scenario 2. This is still within the borrowing headroom based on advice received and is also comparable to other jurisdictions. The debt would be affordable if a "user pays" model was adopted therefore creating an income to cover the cost of the debt. This level of borrowing is, however, significantly more than the limits set in the Fiscal Policy Framework.

16. Sensitivity Analysis

16.1 Medium to long-term financial projections are inherently difficult to predict accurately, especially where there are many variables and key drivers that are subject to change. Although every effort has been made to formulate and produce valid assumptions that will drive as accurate projections as possible, it is essential for sound financial planning that a range of possible outcomes is considered.

Sensitivity of Net Migration Assumption

16.2 The income projections included within the central Scenario, incorporating both General Revenue and Social Security, are based on an assumption of net migration of +150 people a year over the medium term. This is an increase from the +100 assumption used in the previous edition of the F&I Plan and the last actuarial reviews of the Guernsey Insurance and Long term Care Funds.

16.3 This reflects a period of higher than average net migration since 2019, which has increased the average level of net migration experienced over the last 15 years.

16.4 However, this is accompanied by a downward revision of the assumption applied to real earnings growth from RPIX+ 1% to RPIX +0.5% following a period of weak earnings growth in the past 18 months. The impact of these two changes largely cancel each other out.

16.5 In October 2022 (Billet d'Etat XVIII, October 2022) the States resolved:

i. To note the objective findings of the Review, and the evidence presented in sections 5 and 6 of this Policy Letter, that suggests an average net migration level of +300 per year over the next thirty years is required to sustain the Island's workforce at its 2020 level, and to agree that the economic competitiveness of the Island should be supported through the strategic population objective that:

ii. "The States of Guernsey will assume, for the purpose of planning future infrastructure and service provision, that net migration will average up to +300 per year over the next thirty years. This assumption will support the capacity of the Island's workforce so that it remains a desirable and competitive jurisdiction, and will ensure that the Island can meet the needs of the economy with the necessary housing and infrastructure."

16.6 The purpose of this resolution was to ensure that infrastructure is planned and developed to ensure that it has the capacity to meet the needs of the larger population implied by a higher level of net migration. It should also help ensure that the capacity of the Island's infrastructure, and its housing in particular, does not become a barrier to achieving higher levels of net migration.

16.7 However, the actual levels of net migration experienced are cyclical and dependent on a number of factors. The States may have influence over some of these factors, such as the supply of housing and the competitiveness of our tax regime, but over other factors, such as the conditions in global financial markets it has limited control.

16.8 This means that the ambition for higher levels of net migration alone cannot guarantee its delivery. As such at this stage an increase in the central net migration to +300 a year is considered optimistic, given the States has not yet delivered key enabling policies like the Strategic Housing Action and Delivery Plan.

16.9 If Guernsey does see a sustained increase in its level of net migration to the +300 level, this will increase expected revenues, but it will also increase costs. The net gain over the medium term of an increase in net migration assumptions from +150 a year to +300 a year is estimated at around £11m-£17m a year (net of costs) with the benefit divided between General Revenue and the Social Security funds. This would increase the revenues to more in line with the "best case" scenario.

16.10 Conversely a drop down to 100 would reduce revenues by an estimated 0.4%-0.8%

16.11 In addition to this key assumption there could be other changes to the assumptions underpinning the income forecast, such as GDP and earnings growth being higher or lower than modelled.

Best and Worst Cases

16.12 In order to understand the impact of changing key variable a best and a worst-case sensitivity analysis has been prepared on each scenario.

16.13 The worst case assumes the following changes from the middle case:

(a) Income taxes reduce by 1.5%
(b) Customs duties reduce by 2.5%
(c) Document duty income reduces by 10%
(d) Committee Budgets increase by 2.5%
(e) 2023 Budget savings reduce by 33%

(f) States' Trading Assets cost to General Revenue increases by 50%
(g) GWP priorities cost additional 20% per annum
(h) IT resilience cost increase by 40%
(i) Annual savings (in addition to baseline 2023 budget savings) stripped out and assumed at zero
(j) Annual Budget income measures reduce by 50% (£0.5m)
(k) Net income of the tax package reduces by 20%

16.14 The best case assumes the following changes from the middle case:

(a) Income taxes increase by 2.5%
(b) Customs duties increase by 2.5%
(c) Document duty income increases by 10%
(d) Committee Budgets remain as middle case, no improvement
(e) 2023 Budget remain as middle case, no improvement
(f) States Trading Assets cost to General Revenue reduces by 20%
(g) GWP priorities cost 20% less per annum
(h) IT resilience cost remain as middle case, no improvement
(i) Annual savings increased by 63% to reach £16m per annum target by 2029
(j) Annual Budget income measures increased by 50% (£0.5m)
(k) Net income of the tax package increased by 10%

Scenario 3 Best and Worst Cases

16.15 The chart in figure 17 highlights the impact of a change to key assumptions on the Scenario 3 General Revenue surplus (before finance activities). It is shown before financing activities to highlight the underlying financial performance of the States before the highly volatile investment returns, which although remaining stable over the long-term, can swing significantly year on year as was seen in 2021 and 2022.

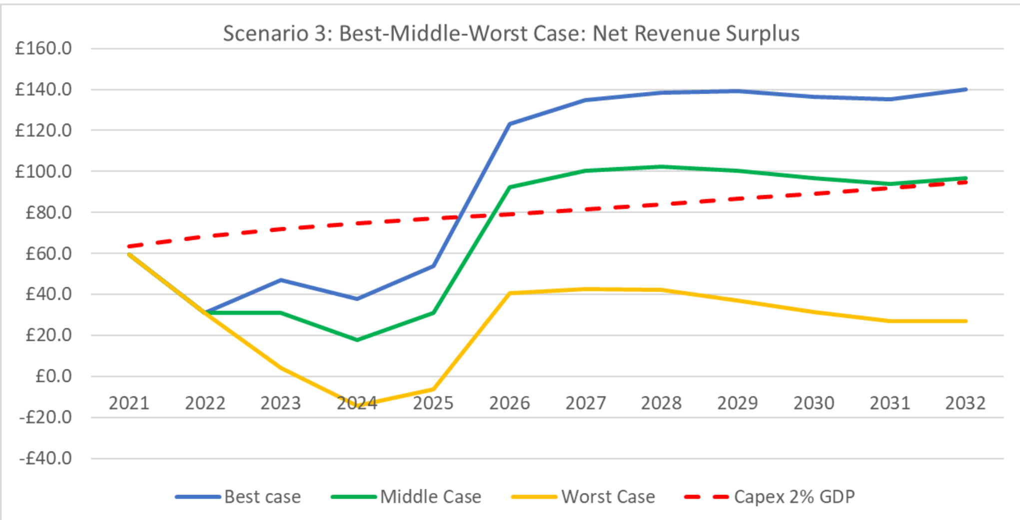


Figure 17

16.16 The difference in the revenue surplus over the 5-year period from 2023 to 2027 between the middle case and worst case cumulatively adds up to £205m. This would mean reserves would decrease by this amount if all of the worst-case assumptions were realised. The best case highlights a potential improvement to the revenue surplus of £125m over the same 5-year period.

16.17 Although it is not likely that all the worst-case assumptions would materialise together, there is a real risk around each of the key variables, and it is therefore prudent to ensure financial planning takes these potential outcomes into consideration.

16.18 The modelling shows that even if all the worst-case assumptions materialise together, the interest payments on the proposed borrowing could still be afforded. However, there would be low remaining revenue surpluses from which to afford future capital investment and to build up reserves.

16.19 The risk that reserves will be utilised quicker than the middle case presents further supports the recommendation to take out additional borrowing to ensure cash reserves are protected.

Scenario 1 and 2 Best and Worst Cases

16.20 The chart in Figure 18 highlights the impact of a change to key assumptions on the Scenario 1 and 2 General Revenue surplus (before finance activities).

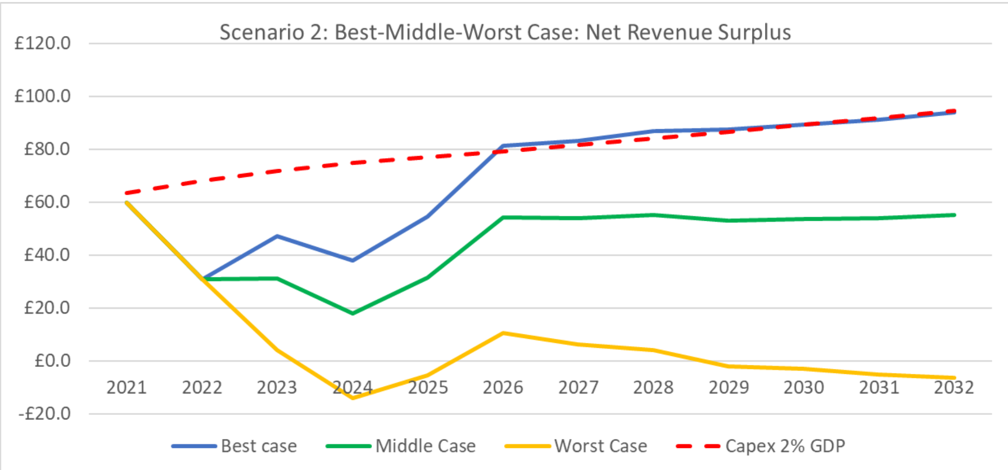


Figure 18

16.21 The best case in this option is financially sustainable, with net revenues in line with the required capital spend at 2% of GDP. However, the worst case shows a significant decline to surpluses resulting in a projected net revenue deficit beyond 2029.

16.22 While the worst-case factors may not all happen at the same time, this demonstrates the lack of financial resilience in Scenarios 1 and 2 compared to Scenario 3 (i.e. without significant additional tax raising).

16.23 Critically, interest payments on the proposed borrowing could not be afforded under this worst-case scenario. Reserves would be depleted by the end of 2029 and the States would very quickly have to develop a strategy to markedly improve the financial position.

17. Risks & Opportunities to this Funding & Investment Plan

17.1 This F&I Plan update is presented at a turning point with the economic outlook looking more positive than it did several months ago. The high level of inflation that appeared throughout 2022 has now begun to fall in Guernsey, albeit more slowly than had been forecast.

17.2 However, there are still many uncertainties resulting in significant risks and opportunities to this F & I Plan.

17.3 While the risk from COVID-19 is now low thanks to the successful vaccination scheme, there may be a future pandemic which presents a risk to the Island's finances. The Bailiwick's successful response to the global pandemic resulted in a better outcome than that seen by other jurisdictions. Yet the cost to the States of the business and payroll support was £73m, and there were further impacts to the States finances owing to poor performance of the trading assets, in particular Guernsey Airport. No costs have been built into the plan for potential future lockdowns, travel restrictions or business support measures.

Inflation

17.4 During 2022, worldwide inflation was very high because of the economic disruption caused by the COVID-19 pandemic and the war in Ukraine. Inflation has started to reduce, but higher inflation in the coming years presents both a risk and an opportunity to the States' financial position.

17.5 Should inflation impact both revenues and expenditure equally, then the impact will be minimal. However, should price inflation increase sharply and revenues not keep pace in real-terms, then it could result in a significant deterioration in the financial position.

17.6 One opportunity, which may arise as a result of higher inflation, is a reduction in the real-terms cost of borrowing, if entered into at a fixed rate of interest.

Interest Rates

17.7 In an effort to control inflation there has been a sharp increase in the Bank of England's base rate. After a decade of very low rates, the base rate has risen rapidly back up to levels that are much more typical in the long term.

17.8 While it is unlikely that rates will fall back to the previous low rates, the interest rate could be higher or lower than that modelled presenting a potential risk or opportunity to this plan.

17.9 A 1% change in the rate has an impact of changing the annual interest payments by c£3.5m for borrowing of £350m borrowing and c£2m for borrowing of £200m.

Investment Return

17.1 The modelling assumes that the rate of investment return is inflation plus 2.5%. While this is lower than the targeted rate of return, it is in line with actual performance and is considered a prudent planning assumption by actuaries.

17.2 In reality, variability year-on-year is expected, as evidenced by the large swings in 2021 and 2022. In addition, the investment return for 2023 to date (to 30 June 2023) is 2.25% which is lower than inflation over the same period and below the target included in the model.

17.3 Figure 19 shows the investment return trend since 2015, illustrating not only the variability but also the average return from 2015 to 2022, which is in line with the planning assumption of inflation plus 2.5%.

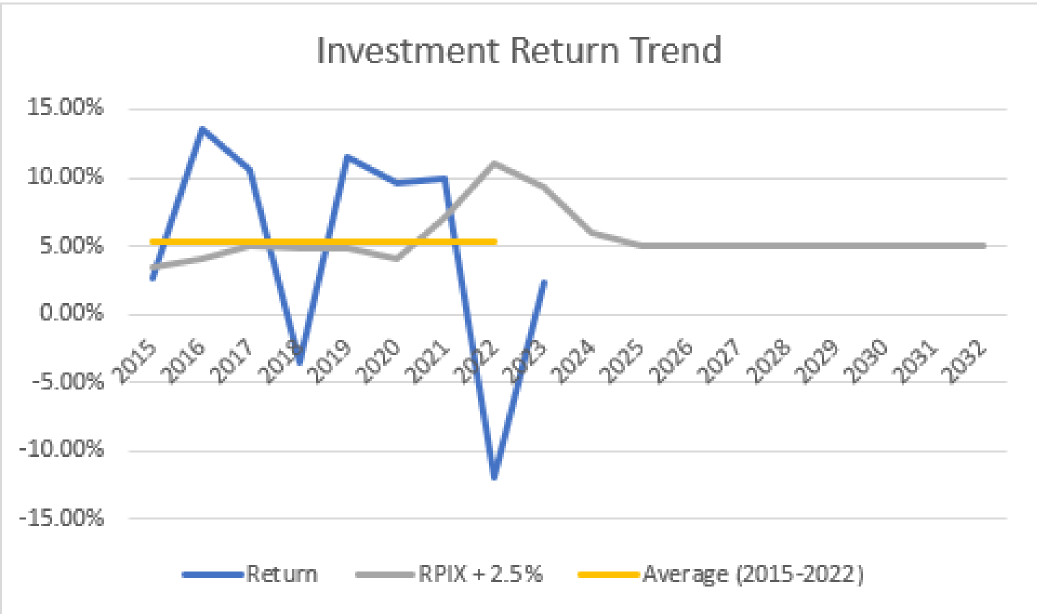


Figure 19

17.4 The rate of investment return in the future is also dependent on the level of reserves. As reserves decrease there is a heighted risk to lower investment returns if the investment strategy needs to change towards a more short-term focus.

17.5 Figure 20 shows the impact of a 1% increase or decrease in the investment return assumption on the 2032 reserves balance for each Scenario.

Modelled Reserves Balance at end 2032 £m	As Modelled (2.5% over Inflation)	1% Increase (3.5% over inflation)		1% Decrease (1.5% over inflation)	
	2032 Closing Balance	2032 Closing Balance	Variance to Model	2032 Closing Balance	Variance to Model
Scenario 1	380	447	67	319	(60)
Scenario 2	277	342	65	219	(58)
Scenario 3	653	737	84	577	(76)

Figure 20

Deliverability of Savings

17.6 Historically the States do not have a good track record of successfully delivering savings targets and there is a significant risk that the £10m savings built into the three scenarios will not be fully realised.

17.7 However, there is also a small upside opportunity if it proves possible to deliver to the upper end of the cost reduction target of £16m.

Additional Unknown Cost Pressures

17.8 There is the risk that baseline costs increase above that provided for in the F&I Plan scenarios. Allowance has been made for any known increases to the cost base already agreed by the States and for future changes in demand for services.

17.9 An example is Health & Social Care where the ageing demographic is having a significant impact on service demand. A £4m per annum real-terms increase to the Health & Social Care baseline costs has been factored into the model based on analysis undertaken internally and as part of the hospital modernisation work, but there is a risk that demand pressures may lead to cost increases in excess of this.

17.10 There will be unknown cost pressures that are not factored into the F&I Plan, and the best- and worst-case scenarios model the impact of costs being higher or lower than the mid case.

Improved Ports Performance

17.1 The F&I Plan factors in an improvement to the Ports' operating deficit. This is currently being reviewed by STSB and figures included in this F&I Plan represent early estimates of the potential recovery. This could present a potential risk that additional funding will be required for the Ports if the recovery cannot be delivered as modelled.

Additional projects not included in the F&I Plan

17.2 While the capital programme has taken account of the prioritised projects at the time of preparation there will be other potential projects which may require funding but are not yet approved.

17.3 For example, the Pool Marina Project which may be approved by the States and require part-funding by the States as well as access to an overdraft or other funding is not currently included in the F&I Plan.

17.4 Other projects that have been highlighted but are not included are a potential project to investigate an offshore wind farm, as well as investment in refurbishment of States Housing.

17.5 There will no doubt be other unforeseen or emergency projects and a contingency for unforeseen and emergency funding has been built in. The contingency is £10m per year in Scenario 3 and £3m per year in Scenario 2.

17.6 Scenario 1 has no contingency for unforeseen projects, representing a real risk that any additional projects in this scenario would require the portfolio to be reprioritised.

Capital prioritisation – Deliverability

17.7 The F&I Plan assumes that the capital portfolio in each case is deliverable from the point of view of both the local construction industry and internal States' resources.

17.8 Both Portfolio 2 and Portfolio 3 represent a challenge with several large schemes planned to run concurrently, including both TEP and OHM phase 2 at their full scope as well as the Children and Families' Hub, Bridge Regeneration - Housing and Flood Defences project and the GHA housing projects. The quantum of construction work planned and profiled for these is ambitious and would include scaling up of the workforce in the construction industry and may place further demand on short to medium term local housing and accommodation.

17.9 Work is ongoing to assess the merits and achievability of a joint construction programme across the Transforming Education Programme – Les Ozouets Campus (LOC) and Our Hospital Modernisation Phase 2 (OHM).

17.10 Portfolio 1 on the other hand may be deliverable but by reducing the pipeline of work from the States it could negatively impact on construction contractor confidence and potentially risk negative economic consequences.

<u>GWP Implementation Costs.</u>

17.11 The GWP includes a range of workstreams which may result in additional cost to the States once policy work is concluded and proposals for changes to service provision are brought back to the States.

17.12 An example is the work to address the long-term care model - SLAWS. The ongoing costs of the existing long term care scheme, and the increased revenues previously agreed by the States to fund this, have been factored into the projections on the LTCF. However, given the extant Resolutions driving this work seek to increase the access to the fund and the range of services available, it is probable that proposals for a new model of care will emerge that increase costs. It has been assumed that any such service change and associated cost increase will be accompanied by proposals for their funding. It is currently planned to return to the States with proposals by end Q2 2024.

17.13 Other examples that may lead to increased costs include the Guernsey Housing Plan, the Health Strategic Portfolio and work around discrimination (equal pay for equal work). All of these could potentially result in higher service delivery costs, although the quantum and likelihood are unknown at this point.

<u>Income</u>

17.14 Income has been forecast on best known information at the time, but there are both risks and opportunities to these projections due to a high number of variables.

17.15 In particular the assumption around real earnings growth could present a risk if earnings growth is lower than inflation.

17.16 The forecast is based on net migration of +150 so there could be either a risk or an opportunity to that assumption depending on the actual working population, as discussed in Section 16: Sensitivity Analysis.

17.17 If there is a prolonged slow-down in the housing market this would present a risk to the projections for document duty.

17.18 There is a risk to the timing of the implementation of any new measures and initiatives, which may take longer than anticipated resulting in the delay of new income streams.

17.19 Opportunities exist for new income generating initiatives and measures not planned for in these projections, such as further corporate taxes, visitor taxes or a health tax or insurance scheme.

Other Economic factors

17.20 The economic environment is both a risk and an opportunity to the projections as recovery and economic growth rates can have a significant impact on General Revenue income.

17.21 An economic shock, such as the collapse of the local banking industry, could have a significant impact on the Bailiwick’s finances, and conversely strong economic performance could present a sizeable boost to General Revenue income.

18. Governance

18.1 The mandate of the Policy & Resources Committee includes setting the framework for the planning, approval and control of public expenditure. The F&I Plan and the annual Budget Reports prepared by the Committee play a pivotal role in ensuring there is a clear and transparent planning framework.

18.2 Following consideration of the GWP, the F&I Plan and any amendments, the States will agree the priorities for the remainder of this political term. They will also agree the funding for these priorities, and the decisions made will have a bearing on the priorities of the next Assembly.

GWP Strategic Portfolio

18.3 Although extensive work has been undertaken in the development of the F&I Plan, many of the resourcing requirements and costings for the GWP strategic portfolio are early, high-level estimates. It has not been possible to verify all costings at this stage and the amounts should be regarded as illustrative only.

18.4 The Committee will ensure that the budgeting framework reflects these priorities and will include appropriate provision for potential funding requirements for the actions included.

18.5 Approval of this F&I Plan does not substitute the need for detailed investment appraisals to ascertain value for money and other benefits ahead of funding approvals.

18.6 The forecast costs set out in this policy letter are best estimates at the time of preparation. Further work will be required to develop more detailed costings for strategic portfolio (GWP) actions before funding requests are made to the Committee, either in year or as part of the budget setting process. The Committee will ensure appropriate and proportionate review and challenge prior to the release and approval of any funding, which will include ascertaining value for money. In addition the review will, where possible, seek clarity over the longer term consequences of any funding requests to ensure the financial implications of such workstreams are fully understood prior to the investment decision. Funding requests are expected to be proportionate and realistic and not include large contingencies.

18.7 The Committee recognises costs are provisional at this stage and that funding requests may be higher or lower than the current figures provided. It also recognises that some of the priorities that currently show no funding required might, in due course, require funding. In reviewing funding requests, the Committee intends to take a pragmatic but robust approach to ensure that it is properly discharging its responsibility for the approval and control of public expenditure.

Capital Portfolio

18.8 The Governance of capital schemes was refined in the 2021 Funding & Investment plan to ensure that there was greater agility in the development of schemes and further strengthen the focus on affordability and public value for money while protecting the States' commercial position which is often compromised by the setting out of project costs in public documents ahead of competitive procurement processes.

18.9 Following debate on that policy letter, the States resolved to give the Policy & Resources Committee delegated authority to approve funding for all schemes in the portfolio up to the maximum costed portfolio value that was set out in Appendix 11.9 of that policy letter[11].

18.10 It was proposed that the level of assurance and reviews and the approvals pathway for each scheme would be agreed at the outset between the sponsoring Committee and the Policy & Resources Committee and captured in a scoping document which would include the scope, goals, objectives and estimated timescales as well as indicative costs. The scoping document also set out any requirement for States' decisions which was dependent on risk, value, public interest and political judgement.

[11] Billet d'État XV, 2021

18.11 Funding approval from the Policy & Resources Committee has been dependent on receiving the necessary assurances that the scheme represents best value and can be delivered according to the approved business case. The Committee has reported back to the States on the use of this delegated authority in the year end accounts, to ensure transparency in the use of public funding.

18.12 In February of this year in the debate on the Tax Review the States resolved to amend that authority so that:

a) in respect of capital votes already opened, the existing agreed approval routes would continue to the completion of those schemes, and
b) in respect of capital votes not yet opened to agree the assurance and approval pathways for capital projects, and to delegate authority to the Policy & Resources Committee to approve the opening of capital votes on projects with an estimated cost of up to £5m.

18.13 The implications are that for this portfolio, any projects with an estimated cost of over £5m, and without a current open vote, the project would be required to return to the States for approval, if accepted in the portfolio following the debate on this F&I Plan.

18.14 For the portfolio proposed in Scenario 3 it would mean the following projects would be required to return to the States for approval prior to any financial commitments being made or the procurement process started. It should be noted that this could compromise commercial negotiations and so sponsoring Committees should consider the level of detail provided any policy letters and consider how much of detail provided in the business case is published.

c) Central Stores (if over £5m)
d) Repair/Replacement of Castle Emplacement Bridge
e) Future Inert Waste Facility
f) Community Services Children & Families' Hub
g) Bridge Regeneration (Housing and Flood Defences)

18.15 For all other projects there would be no requirement to return to the States for approvals, but P&R and sponsoring committees may choose to do so. The Committee will continue to ensure that all funding requests are subject to appropriate and proportionate review and governance, ensuring best practice methodology for project and business case development, including costing and risk management (application of HM Treasury Green Book). All capital and transformation projects will be subject to the same scrutiny and governance processes before the release of any funding.

ANNEX 2: CAPITAL PORTFOLIO REVIEW

1. Background

1.1 The development of the capital portfolio is undertaken at the beginning of each political term and includes a range of projects and programmes investing in infrastructure and systems, ultimately supporting the Bailiwick's economic activity and overall recovery post pandemic.

1.2 Together with the Funding & Investment Plan ("the F&I Plan"), the objective is to ensure that investment is affordable, deliverable, and aligned with the States' strategic objectives and priorities. This is balanced with investment in maintaining public services through the replacement of core assets and compliance activities.

1.3 The current portfolio, developed following a thorough prioritisation approach, was approved by the States as part of the Government Work Plan (GWP)[1] and therefore all existing schemes have already been prioritised and have merit.

1.4 The portfolio has two categories of schemes:

- **Delivery**: containing schemes that are planned to **commence delivery before the end of this political term**, and;

- **Pipeline:** containing schemes requiring development work and likely to **commence after this political term.** The purpose of including pipeline schemes is to seek to extend the planning horizons and ensure that schemes are ready to commence detailed planning work / delivery in the next portfolio period, subject to prioritisation. Those schemes identified as pipeline can access funding to commence preliminary work to provide clarity in terms of direction and scope.

1.5 Within the overall portfolio amount, a provision of £25m was also included to be able to respond to emergency funding requests and/or new opportunities supported by a strong business case.

1.6 In addition to the major capital portfolio, the States also have a portfolio of minor capital projects for routine investment in assets including critical infrastructure. Allocations are made on a multi-year basis to facilitate the development of rolling replacement, maintenance, and improvement programmes. These schemes are managed alongside the major capital portfolio as both put pressure on the availability of the supplier market and internal resources. The States of Guernsey

[1] Billet d'État XV, 2021

Annual Budget for 2021[2] set minor capital funding for the period 2021 – 2024 to align with the major capital portfolio time-period:

- Information Technology - £11.7m
- Medical Equipment - £10m
- Vehicles & Other Equipment - £10m
- Property Maintenance and Minor Works - £21.8m
- Property Maintenance: Roads resurfacing programme - £10m
- Implementation of the Integrated Transport Strategy - £1m
- Coastal repairs - £3.8m

2. Changing Context

2.1 Over the last two years the context for affordability and delivery have changed. The significant challenges currently faced include:

- **Scheduling:** There are several complex programmes and projects which have had to be re-scheduled and are now expected to be delivered within similar time frames in an already stretched operational (business as usual) environment.

  There are large programmes of work to support the Transforming Health & Social Care and Transforming Education Programmes within the portfolio, alongside significant minor capital activity. The build schedules for these programmes are therefore a key consideration in the deliverability of the portfolio.

- **Limited resources:** Linked to the scheduling challenges above, the organisational capacity and capability to develop, manage and deliver the large number of high-risk projects and programmes which are maturing at the same time within the portfolio is challenging. This includes specialist skills such as: project and programme management: change management; IT; and procurement / commercial specialisms. The concurrent demand for these skills externally and internally is therefore higher than anticipated, coupled with the scarcity of some skills on Island.

  It is critical that the major capital schemes are internally led to ensure that value for money is given as much focus as successful completion. However, at a strategic level, the organisation needs to ensure that the range of critical portfolio schemes is manageable.

[2] Billet d'État XXVI, 2020

It should also be noted that there are several other initiatives outside the capital portfolio that are in flight or being planned, including a range of MoneyVal priorities and the broader delivery of the current GWP policy priorities, which may lead to further programme and project resource requirements over time, increasing pressure on scarce resources. It is important therefore that the capital portfolio is not viewed in isolation.

- **Construction market capacity:** The intention to support local employment by investing within the Bailiwick is noted within the GWP and is a key feature of the States' procurement policy. To maximise this, the scheduling of projected capital projects needs to be managed so as not to over-heat the local market.

  Success in delivering the proposed investments in infrastructure requires careful planning and phasing with the supplier market. There is a need to balance cost, time, quality, and service risk at a portfolio level and this may require projects to be accelerated or paused depending on supplier availability.

  Maintaining a pipeline of ongoing investment in critical infrastructure is important to the supply market as this ensures confidence and encourages continued investment in maintaining key skills, which benefits the wider economy. The States' infrastructure projects often have specific construction or civil engineering requirements (schools, hospitals, bridges, cliff faces etc.) which are quite different in their requirements to a residential or office build. These schemes draw on skills which are in short supply in Guernsey which makes the pipeline important if the island is to maintain relevant competencies and capacity. Likewise, an agreed and evenly spread portfolio ensuring a steady stream of projects into the sector is preferable as this keeps demand and supply stable and prevents the potential risk of either different Committees competing for the same capacity or the market facing a shortfall in demand and therefore contracting.

- **Affordability factors:** The estimated cost of the current portfolio has increased significantly since estimates were compiled during the prioritisation exercise in 2020 and 2021. This is owing to a combination of higher-than-expected construction inflation rates; increases in resource costs; schemes developing detailed plans and therefore being able to provide greater certainty on costs; and some scope changes.

3. The Major Capital Portfolio Review

3.1 Following consideration of The Tax Review: Phase 2[3] the States resolved to:

Direct the Policy & Resources Committee through engagement with Principal Committees and wider States' Members to review the Capital Portfolio and pipeline in light of the outcome of the debate and report back to the States by March 2024 with recommendations for:

i. any changes to the scope or funding of the existing portfolio;
ii. alternative funding mechanisms including borrowing; and
iii. (If in the view of the Policy & Resources Committee thought appropriate) amending the assumption for the level of capital expenditure contained within Principle 6 of the Fiscal Policy Framework.

3.2 Following the debate, the Policy & Resources Committee reviewed all the Resolutions and agreed how to progress them. The Committee noted that the total estimated cost to completion of the current capital portfolio would result in the balances of available reserves being completely exhausted. Therefore, it determined that it would be prudent to consider significantly reducing the size of the capital portfolio to protect reserves given there was little likelihood of any significant additional revenue raising ahead of the next political term.

3.3 Given the uncertainty created by the Resolution and the number of programmes already under way which would be seeking funding in the immediate future, it was determined that it was neither practical nor realistic to wait until March 2024 to report back on this matter. The review was therefore set as a top priority.

3.4 In March 2023, the Policy & Resources Committee wrote to all Principal Committees setting out the proposed review. The letter confirmed that it would not be possible to approve any substantial increases to capital votes pending the outcomes of the review and decisions on the future portfolio. Only small funding requests have been considered in the interim that are felt to be critical or for work which would still have value even if the scheme was delayed, suspended, and/or removed.

3.5 Work commenced shortly after, as directed by the Committee, including a multi-disciplinary workshop comprising a range of senior officers held on 15 March.

[3] Billet d'État III, 2023

3.6 During this workshop each scheme was reconsidered within the context of the States' strategic objectives; impact; overall risk; likely benefits; available resources; contractual commitments; criticality; scale of investment; value for money; timing; and stage of development. Updated scheme information was used alongside an understanding of what has changed since the portfolio was first approved by the States in 2021.

3.7 The emphasis was not on starting again given that the current portfolio had been carefully prioritised in line with the GWP guiding principles and priorities, but to respond to the shifts that had occurred in the first two years of the political term.

3.8 The review categorised schemes as one of the following:

- **In flight** – schemes that have already had substantive investment, are being delivered or are near completion. The funding for these schemes is therefore committed.

- **Do as planned** – schemes that are categorised as in delivery or are proposed to progress to substantive investment decision and contract award in this political term as planned.

- **Do but review scope and / or solution** – schemes where there is potential to take a fresh look at the options: i.e., looking at the scale of the scheme or revisiting core requirements within affordability parameters. This does not represent small tweaks to the original solution but is essentially scaling back projects to make them affordable and deliverable.

- **Pipeline** – schemes which should be subject to prioritisation in future political terms.

3.9 The outputs of this work were presented to the Policy & Resources Committee along with recommendations for portfolio changes. Following review and challenge, the Committee then made an initial determination of proposed changes which was communicated to Principal Committees.

3.10 A series of engagement meetings with Principal Committees to discuss proposals and invite feedback were then commenced covering both the capital portfolio schemes and the GWP priorities.

3.11 Additional meetings were organised with the Committee *for* Health & Social Care (C*f*HSC) and the Committee *for* Education, Sport & Culture (C*f*ESC) due to the potential impact on two of the largest and most complex capital schemes.

3.12 At the end of the review process, a seminar for all States Members to discuss the findings was held in May 2023.

3.13 The above review and engagement have informed the portfolio options set out below.

4. Proposed Portfolio Options

Proposed New Schemes Common to all Options

4.1 The GWP was agreed in July 2021 against a backdrop of pandemic recovery and since then the States have had to adapt to significant local, national, and global challenges. The impacts of such rapid change has had a significant effect on the cost of living and housing; the local economy including recruitment; government finances; and many other areas.

4.2 In their mid-term GWP reset in July 2023, the States agreed in principle three strategic portfolios for the remainder of this term. Housing supply and affordability was central to each as increased housing supply will support the delivery of public services by providing accommodation for key workers. It will help to mitigate against the cost of living by providing more affordable housing and support economic growth and competitiveness.

4.3 In response concerns raised by the Assembly expressed over the continued pressure on housing, the Committee has prioritised housing supply and affordability in the 'economy focused' strategic portfolio. The Committee is also now proposing that an additional scheme is added to the capital portfolio to support the regeneration of the Bridge through housing and associated flood defences. This scheme has been included in each of the three capital portfolio options which follow.

4.4 In line with the Resolution of the States [4], funding is also prioritised to progress surveys to conclude the option appraisals for the future of the island's harbours, essential to secure the delivery of the commodities the community needs. This strategic alignment underpins each of the following three capital portfolio options for the States to consider.

4.5 In recognition of the above developments, two additional schemes have been included in all the proposed portfolios:

- Bridge Regeneration (Housing) and associated flood defences
- Future Harbour Requirements - survey work

[4] Billet d'Etat VI, March 2022

Removed Schemes

4.6 On the advice of the Committee *for* Economic Development, the following schemes have been de-prioritised and removed from all three portfolio options:

- Territorial Seas and Fisheries Enforcement - on the basis that £300K of funding is made available from minor capital to keep the Leopardess in operation; and
- Guernsey Tourism Product Development.

In Flight Schemes

4.7 Since the approval of the major capital portfolio in 2021, many of the schemes have progressed and may have already had substantive investment, are being delivered, are near completion and/or have a contractual agreement in place. Funding is therefore committed.

4.8 These schemes are being categorised as 'in flight' and are included in all the portfolio options which follow:

- Our Hospital Modernisation Phase 1
- Electronic Patient Record
- Digital Infrastructure
- Funding Affordable Housing Developments Programme
- IT Transformation
- Revenue Service Programme
- VME Replacement
- Guernsey Registry IT Systems Replacement
- Online Passport & Workflow System
- Footes Lane Refurbishment (near completion)
- Sarnia Cherie BWMS (near completion)
- Mont Crevelt Breakwater Reinstatement
- Transforming Education Digital (secondary and primary)
- SMART Court Phase 1
- MyGOV Programme (near completion)
- Havelet Slipway Repairs
- Tetra PSN

Portfolio Options

4.9 The Committee has developed three different portfolio options which have been determined based on the funding available under the three funding scenarios set out in the F&I Plan. It should be noted that in all cases, the funding required represents the remaining cost from 2023 to scheme completion.

- **Portfolio 1** – A significantly reduced portfolio totalling £190m which is deliverable within existing financial resources and with no new borrowing as part of Scenario 1 in the F&I Plan.

- **Portfolio 2** – A deliverable and affordable portfolio based on the Committee's initial proposed portfolio communicated in March 2023 but adjusted for recent developments.

  This portfolio totals £440m and would require borrowing of £200m as well as use of the remaining Health Service Reserve as set out in Scenario 2 of the F&I Plan.

- **Portfolio 3** – This portfolio has been derived following the full review based on States' priorities and accommodating requirements of Principal Committees and recent developments.

  This portfolio totals £520m and would require borrowing of £350m as set out in the F&I Plan Scenario 3.

4.10 Further detail on all portfolios follows in Sections 5, 6 and 7 and are illustrated in Appendix 5.

5. Portfolio 1

5.1 This portfolio significantly reduces investment in the States' critical infrastructure in this term. This reduction would bring the total investment over the remainder of this term down to approximately 2% of GDP.

5.2 Given the limited funding, most schemes included in this portfolio are those categorised as 'in flight'.

5.3 The portfolio also takes account of schemes that are essential for the States to comply with laws and regulations; the solution for these schemes may be variable but the outcome of being compliant is fixed and therefore deemed necessary:

- Future Harbour Requirements – Survey Work - recognises the States' recent Resolution following consideration of the East Coast Development[5] and the pressing need to finalise plans for the lifeline harbours through which the Bailiwick's essential commodities are transported.

[5] Billet d'État X of 2023, Article 14

- Bridge Regeneration (Housing) and associated Flood Defences. This scheme accelerates the St Sampson's harbour bridge flood defence work which is part of the much broader Coastal Flood Defences scheme. The Committee is progressing discussions and subject to ongoing due diligence and assurance, it intends to bring proposals to the States in November for the December 2023 States Meeting.

- Community Services - Children and Families Hub – accelerating part of the overall Community Hub scheme scope. The Children and Families Hub includes early intervention and wrap-around services for families, recognising the operational importance of co-locating States' services whilst also securing capital receipts by vacating, and then disposing of, several buildings.

  This scheme was previously included as part of the scope of the Community Hub in the 'pipeline' and is recommended to move to delivery in all portfolio options because the scheme is sufficiently mature in its planning to progress now. As a result, the States are therefore likely to benefit from service benefits and capital receipts sooner than originally anticipated.

- Clinical and Animal Waste Solution - a compliance scheme considered necessary to provide a facility that meets current environmental standards.

- Supply Chain Relocation (Central Stores) – an enabler to achieve operational and revenue efficiencies and critical enabler required ahead of any future redesign of the Princess Elizabeth Hospital (OHM Phase 2). This scheme was previously included within the OHM programme but is proposed as a separate scheme to recognise the broader emphasis beyond health.

- Fermain Wall Repair – This is a proposed reduction in scope which originally included the repair of the collapsed wall at Fermain. Work to the coastal path is necessary to continue to allow safe access by the public but repair of the collapsed wall itself is not necessary from a coastal repair perspective. Therefore, this project now includes realignment of the public cliff path only.

- Guernsey Airport Pavement Rehabilitation (PFOS) – a compliance scheme to transfer contaminated soils from the Island to a processing plant in the UK or Europe to meet environmental standards for which the States of Guernsey are under Notice.

- Property Rationalisation Phase 2 – which will continue to rationalise the estate for efficiencies/income generation through the release of capital assets.

- Repair/Replacement of Castle Emplacement Bridge - recognising the need for urgent works to continue to provide access to Castle Cornet and the lighthouse.

- Alderney Airport Pavement Rehabilitation – to repair and extend the runway and modernisation of the terminal and other buildings in conjunction with the States of Alderney to support rationalisation of the Aurigny fleet.

5.4 The following schemes that were originally categorised as ‘delivery’ are now unaffordable within this funding scenario. It is likely that removing these schemes to pipeline will prolong the need for services to use short term mitigation plans which may increase revenue costs (which have been modelled in the F&I Plan where quantifiable) and lead to other unavoidable capital costs:

- Transforming Education Programme (TEP) – which includes the Les Ozouets Campus construction project to deliver a higher education facility. However, this excludes the Digital Programme for secondary and primary schools which is in flight.

- Our Hospital Modernisation (OHM) Phase 2 and associated works and the Pathology scheme – the remaining hospital redesign which also impacts realising the full benefits of Phase 1 investment.

- Future Inert Waste Facility – which includes the scoping, planning and implementation of a future inert waste disposal facility. This is dependent on a future policy decision of the States with regard to the future use of Les Vardes Quarry.

  As a pipeline project, the work can continue on scoping the facility, but the operational impact of delay is the build-up of inert waste and significant costs for double handling. The States’ Trading Supervisory Board (STSB) highlights that while the scheme is not likely to mature sufficiently to request substantive funding in this political term, the longer the solution takes to deliver, the greater the cost to the Island because of the need to double handle the waste. Whatever option is chosen, there will be a requirement to stockpile and double handle inert waste until a new facility is operational. The actual level of stockpiling and the associated financial implications will be directly linked to the identification of the best practicable environmental option and the selected solution’s implementation timeline.

- Bus Fleet Replacement Phase 3 – to purchase eight replacement vehicles to complete the replacement programme and to support future public and education transport requirements.

- SAP Roadmap – updating the organisation's core systems including payroll, recruitment, and vendor management.

- SMART Court Phases 2 & 3 – aimed at enabling more efficient services to be provided from the Greffe, HM Sheriff and Sergeant, and Registrations departments through digital and information technologies.

5.5 The following schemes also remain in the pipeline category:

- CCTV Replacement
- Coastal Flood Defences
- Guernsey Runway Infrastructure
- Home Affairs Estate Rationalisation
- Community Hub Phase 2 – (Health and Social Care)
- HSC Digital Roadmap
- Future Guernsey Dairy
- Future Harbour Requirements

5.6 A provision of £1m has been made within this portfolio option to support the development of pipeline schemes, this being all that is affordable.

6. Portfolio 2

6.1 This portfolio is an evolution of that first discussed with Principal Committees in March 2023. It reduces the capital portfolio investment required by c£40m compared with the current estimated cost of the original 2021 portfolio**.**

6.2 The major change now being proposed is the following significant projects are to be included as **'do as planned'** at their full estimated investment levels:

- TEP – delivering a transformed education operating model; improving educational assets including the Les Ozouets Campus construction project; and delivering improvements to the way education is governed.

  Including the scheme recognises the significant disruption already experienced by pupils and the maturity of the formal consultation with staff, which, if halted or unpicked, would pose significant risk for the education service.

- OHM Phase 2 and associated works - recognising this phase realises benefits such as delivering capacity to deal with the well documented rising waiting lists (and associated costs of not providing timely treatments); health complexity associated with the Bailiwick's ageing demographic; and addresses known risks including those that arise from departments not being sufficiently close to each other e.g. between maternity and theatre.

6.3 Other changes include:

- Bus Fleet Replacement Phase 3 and SMART Court Phases 2 & 3 are categorised as 'review of scope and/or solution'. This is to ensure that they are both focused on core requirements and consider alternative ways of addressing the problems.

- The Future Inert Waste Facility, Pathology Services and the SAP Roadmap are included as 'pipeline' schemes as they are also unaffordable within the available funding.

6.4 It is acknowledged that Portfolio 2 will be more challenging than Portfolio 1 to deliver, but work is ongoing to assess the merits and achievability of a joint construction programme across the TEP – Les Ozouets Campus (LOC) and OHM Phase 2 and associated works. This workstream has sought to test the capacity of the local supply chain to service the scale of work required if construction work is started in the next two years. Staggering timelines within a combined schedule appears to mitigate deliverability concerns as projects will not pull on the same trades at the same time.

6.5 It is also worth noting that this review does, as far as possible, consider other construction activity in the private development market which will have an influence on capacity. Consideration is being given to achieving this alongside:

- The Affordable Housing Development Programme (AHDP) delivered by the Guernsey Housing Association (GHA); at present this comprises seven prioritised development sites with a current estimated yield of 415 housing units.

- Bridge Regeneration Housing and Flood Defences (BRH) capital project for housing units and to provide sufficient protection from the risk of overtopping at St Sampson's Harbour.

Each has an influence on demand but may provide opportunity to scale up small to medium sized construction companies to meet capacity requirement therefore diversifying the on-island construction market.

6.6 A provision of £2.5m is included to progress pipeline schemes with this option.

7. Portfolio 3

7.1 Following the full review based on the States' priorities accommodating requirements of Principal Committees and assessing the impact of operating constraints, this portfolio allows the broadest range of investment in the delivery category and future substantive investment in the pipeline schemes.

7.2 In addition to schemes included in Portfolio 2, this portfolio enables continuation of the Future Inert Waste Facility and SAP Roadmap as 'do as planned' schemes in the portfolio at their full estimated investment levels.

7.3 A provision of £5m has been included within this portfolio to progress pipeline schemes.

8. Portfolio Summary

8.1 The three portfolios are summarised in the table below. This does not include schemes that are in flight which are consistent across all portfolio options.

Table 1 –Portfolio summaries

Portfolio 1	Portfolio 2	Portfolio 3
Do As Planned	**Do As Planned**	**Do As Planned**
Property Rationalisation Phase 2	Property Rationalisation Phase 2	Property Rationalisation Phase 2
Clinical & Animal Waste Solution	Clinical & Animal Waste Solution	Clinical & Animal Waste Solution
Community Services - Children & Families Hub	Community Services Children & Families Hub	Community Services Children & Families Hub
Central Stores - Supply Chain Relocation	Central Stores - Supply Chain Relocation	Central Stores - Supply Chain Relocation
Bridge Regeneration (Housing and SS Bridge Flood Defences)	Bridge Regeneration (Housing and SS Bridge Flood Defences)	Bridge Regeneration (Housing and SS Bridge Flood Defences)
Future Harbour Requirements - Survey	Future Harbour Requirements - Survey	Future Harbour Requirements - Survey
Alderney Airport Pavements Rehabilitation	Alderney Airport Pavements Rehabilitation	Alderney Airport Pavements Rehabilitation
Repair/Replacement of Castle Emplacement Bridge	Repair/Replacement of Castle Emplacement Bridge	Repair/Replacement of Castle Emplacement Bridge
	Our Hospital Modernisation Phase 2 and associated works	Our Hospital Modernisation Phase 2 and associated works
	Transforming Education Programme	Transforming Education Programme
		SAP Roadmap
		Future Inert Waste Facility

Portfolio 1	Portfolio 2	Portfolio 3
Do But Review Scope &/or Solution	**Do But Review Scope &/or Solution**	**Do But Review Scope &/or Solution**
Guernsey Airport Pavements Rehabilitation (PFOS)	Guernsey Airport Pavements Rehabilitation (PFOS)	Guernsey Airport Pavements Rehabilitation (PFOS)
Fermain Wall Repair	Fermain Wall Repair	Fermain Wall Repair
	Bus Fleet Replacement Phase 3	Bus Fleet Replacement Phase 3
	SMART Court Phases 2 & 3	SMART Court Phases 2 & 3

Portfolio 1	Portfolio 2	Portfolio 3
Pipeline	**Pipeline**	**Pipeline**
CCTV Replacement	CCTV Replacement	CCTV Replacement
Coastal Flood Defences	Coastal Flood Defences	Coastal Flood Defences
Guernsey Airport Runway Infrastructure	Guernsey Airport Runway Infrastructure	Guernsey Airport Runway Infrastructure
Home Affairs Estate Rationalisation	Home Affairs Estate Rationalisation	Home Affairs Estate Rationalisation
Community Hub (Health and Social Care)	Community Hub (Health and Social Care)	Community Hub (Health and Social Care)
HSC Digital Roadmap	HSC Digital Roadmap	HSC Digital Roadmap
Future Guernsey Dairy	Future Guernsey Dairy	Future Guernsey Dairy
Future Harbour Requirements	Future Harbour Requirements	Future Harbour Requirements
Our Hospital Modernisation - Pathology	Our Hospital Modernisation - Pathology	Our Hospital Modernisation - Pathology
SAP Roadmap	SAP Roadmap	

Portfolio 1	Portfolio 2	Portfolio 3
Future Inert Waste Facility	Future Inert Waste Facility	
Our Hospital Modernisation Phase 2 and associated works		
Transforming Education Programme		
Bus Fleet Replacement Phase 3		
SMART Court Phases 2 & 3		

9. Funding requirements across portfolios

9.1 The following table sets out the funding requirements for each of the portfolios as well as the baseline position. The figures presented in the table are based on the most current information and are the costs to completion (not including costs already incurred).

9.2 The 'next term provision' within the table includes an indicative funding provision for future portfolios over the remainder of the 10-year F&I Plan period. This is set at 2% of GDP per annum in line with the Fiscal Policy Framework. This number varies between the portfolios to reflect the overall expenditure in any one year – since the expenditure on the three portfolios continues beyond the end of this term, an amount has been assumed to make up the full amount to 2% of GDP.

Table 2 – Funding required per portfolio.

Funding Required 2023-2025 £M	Current Portfolio	Portfolio 1	Portfolio 2	Portfolio 3
Major Capital	469	189	427	487
Minor Capital	62	64	62	62
Urgent & Unplanned	31	-	13	34
Transformation	25	13	25	25
Total Capital & One-Off	**587**	**266**	**527**	**608**
% GDP	**3.8%**	**2.2%**	**3.8%**	**4.1%**

9.3 Within each scenario an amount of funding has been assumed for transformation projects. This funding is used to drive change across government services rather than procuring or developing an asset. A provision has been made this term for projects focusing on transforming the following areas:

i. Education
ii. Health & Social Care
iii. Digitisation of government services

Due to affordability constraints, Scenario 1 has restricted the amount of funding available for the remainder of this term to £13m.

10. Summary

10.1 This report has presented three options for the major capital portfolio for the remainder of this political term, each building on the previous option and designed to fit with different funding scenarios set out in the F&I Plan.

10.2 Portfolio 1 addresses the identified affordability constraints and will significantly lessen pressures on the construction market and key resources. However, this portfolio omits some of the previously prioritised key infrastructure priorities which will create additional risk for the States, potentially necessitate spend on assets which are planned to be disposed of, as well as limiting the realisation of expected benefits.

10.3 In addition, with limited pipeline funding, this option would constrain the ability to develop the deprioritised projects and other key pipeline projects in a timely way potentially having a knock-on implication for the continuity of future development and investment.

10.4 There is no unforeseen contingency in Portfolio 1, so in the event of an emergency project, another project would need to be removed for the portfolio to remain affordable.

10.5 Portfolio 2 seeks to deliver more of the Bailiwick’s prioritised critical infrastructure schemes but in turn adds pressure on capacity constraints. It comes with greater deliverability challenges than Portfolio 1, but these are judged to be manageable with careful scheduling of work.

10.6 Assessing scheduling timelines for two of our major programmes alongside other infrastructure schemes is likely to improve the deliverability of the construction elements of the portfolio by flattening demand in the next two years in a restricted supplier market.

10.7 Portfolio 3 is unlikely to add significant additional deliverability pressures compared to Portfolio 2 as the Future Inert Waste Facility is likely to require a specialist contractor. The inclusion of the SAP Roadmap scheme is likely to require significant internal resource to be allocated and the availability of such resource needs to be carefully planned. As with Portfolio 2, careful scheduling of schemes will be critical to successfully delivering the portfolio ambitions.

10.8 There has been substantial historic underinvestment in public infrastructure and assets resulting in a significant number of necessary schemes now requiring investment. Portfolio 1 provides the absolute minimum (mainly to ensure compliance) investment required but simply creates a further backlog for future States. Portfolios 2 and 3 both address an element of the backlog and ensure investment in necessary public assets in the short term and are recommended to the States.

APPENDIX 1

Proposition Details for each Scenario

This appendix describes the revenue raising measures, cost reduction targets and capital portfolios related to each proposition of the Funding & Investment Plan .

Proposition 1: Core Measures

1) The introduction of taxes on transport raising an estimated £10m per annum.

2) The application of the OECD Pillar 2 initiative applying an effective rate of tax of 15% to companies with global revenues of more than €750m from 2025 raising a minimum of £10m per annum.

3) Further measures to increase revenues from the corporate sector through a levy or other measures totalling an estimated £5m per annum.

4) Cost savings targets of £10m to be delivered in a phased approach by end 2028.

5) The delivery of the following 17 'in-flight' capital projects at a cost of £96m:

- Our Hospital Modernisation Phase 1
- Electronic Patient Record
- Digital Infrastructure
- Funding Affordable Housing Developments Programme
- IT Transformation
- Revenue Service Programme
- VME Replacement
- Guernsey Registry IT Systems Replacement
- Online Passport & Workflow System
- Footes Lane Refurbishment
- Sarnia Cherie BWMS
- Mont Crevelt Breakwater Reinstatement
- Transforming Education Digital (secondary and primary)
- SMART Court Phase 1
- MyGOV Programme
- Havelet Slipway Repairs
- Tetra PSN

APPENDIX 1

Proposition 2: Scenario 3

In addition to the core elements listed above Scenario 3 includes the following**:**

1) The application of a progressive package of tax measures as described in detail in Billet d'État II, January 2023 raising an estimated £59m (vs 2023 baseline) incorporating:

    - The application of a lower rate of personal income tax at 15% to income up to £30,000.
    - A £600 increase in the personal income tax allowance.
    - The restructure of the Social Security contributions system to apply an allowance and align the definition of income for all contributors (requiring an increase in rates to compensate for the lost revenues) and the application of a 2% rate for employers on the income earned by their employees between the Upper Earnings Limit and £250,000.
    - The application of a broad-based GST.
    - An increase in pensions and benefits sufficient to cover the estimated impact of the GST on inflation, applied before the application of the GST.

2) A cost support scheme available to low-income households who are not in receipt of income support at an initial rate of £450 for a single adult and £675 for a couple.

3) A capital portfolio with an estimated total cost of £520m from 1st January 2023 to completion, including £5m for pipeline schemes and £30m for an unforeseen contingency. Schemes included in this portfolio in addition to core:

    <u>Do As Planned (£379m):</u>

    - Property Rationalisation Phase 2
    - Clinical & Animal Waste Solution
    - Community Services Children & Families Hub
    - Central Stores - Supply Chain Relocation
    - Bridge Regeneration (Housing and SS Bridge Flood Defences)
    - Future Harbour Requirements - Survey
    - Alderney Airport Pavements Rehabilitation
    - Repair/Replacement of Castle Emplacement Bridge
    - Our Hospital Modernisation Phase 2 and associated works
    - Transforming Education Programme
    - SAP Roadmap
    - Future Inert Waste Facility

Do But Review Scope &/or Solution (£10m):

- Guernsey Airport Pavements Rehabilitation (PFOS)
- Fermain Wall Repair
- Bus Fleet Replacement Phase 3
- SMART Court Phases 2 & 3

Pipeline (£5m):

- CCTV Replacement
- Coastal Flood Defences
- Guernsey Airport Runway Infrastructure
- Home Affairs Estate Rationalisation
- Community Hub (Health and Social Care)
- HSC Digital Roadmap
- Future Guernsey Dairy
- Future Harbour Requirements
- Our Hospital Modernisation – Pathology

4) Transformation projects with an estimated cost of £25m to end of 2025, including:

- Transforming Health & Social Care
- Transforming Education
- MyGov – Transforming Government Services – Next Phase

Proposition 3: Scenario 2

1) A continued increase in the contributions rates over ten years to fund the Guernsey Insurance Fund and the Long-Term Care Fund as per the in-principle decision made by the States in October 2021 raising a further £29m (noting that a subsequent proposal by the Committee for employment & Social Security to restructure these contributions while raising an equivalent amount of revenue may follow)

2) A capital portfolio with an estimated total cost of £440m from 1st January 2023 to completion, including £2.5m for pipeline schemes and £12.5m for an unforeseen contingency. Schemes included in this portfolio in addition to core:

Do As Planned (£319m):

- Property Rationalisation Phase 2
- Clinical & Animal Waste Solution
- Community Services Children & Families Hub
- Central Stores - Supply Chain Relocation
- Bridge Regeneration (Housing and SS Bridge Flood Defences)

- Future Harbour Requirements - Survey
- Alderney Airport Pavements Rehabilitation
- Repair/Replacement of Castle Emplacement Bridge
- Our Hospital Modernisation Phase 2 and associated works
- Transforming Education Programme

<u>Do But Review Scope &/or Solution (£10m):</u>

- Guernsey Airport Pavements Rehabilitation (PFOS)
- Fermain Wall Repair
- Bus Fleet Replacement Phase 3
- SMART Court Phases 2 & 3

<u>Pipeline (£2.5m):</u>

- CCTV Replacement
- Coastal Flood Defences
- Guernsey Airport Runway Infrastructure
- Home Affairs Estate Rationalisation
- Community Hub (Health and Social Care)
- HSC Digital Roadmap
- Future Guernsey Dairy
- Future Harbour Requirements
- Our Hospital Modernisation – Pathology
- SAP Roadmap
- Future Inert Waste Facility

3) Transformation projects with an estimated cost of £25m to end of 2025, including:

- Transforming Health & Social Care
- Transforming Education
- MyGov – Transforming Government Services – Next Phase

Proposition 4: Scenario 1

1) A continued increase in the contributions rates over ten years to fund the Guernsey Insurance Fund and the Long-Term Care Fund as per the in-principle decision made by the States in October 2021 raising a further £29m (noting that a subsequent proposal by the Committee for employment & Social Security to restructure these contributions while raising an equivalent amount of revenue may follow).

2) A capital portfolio with an estimated total cost of £190m from 1st January 2023 to completion, including £1m for pipeline costs but no 'unforeseen' provision. In addition to core the schemes included in this portfolio are:

Do As Planned (£88m):

- Property Rationalisation Phase 2
- Clinical & Animal Waste Solution
- Community Services Children & Families Hub
- Central Stores - Supply Chain Relocation
- Bridge Regeneration (Housing and SS Bridge Flood Defences)
- Future Harbour Requirements - Survey
- Alderney Airport Pavements Rehabilitation
- Repair/Replacement of Castle Emplacement Bridge

Do But Review Scope &/or Solution (£5m):

- Guernsey Airport Pavements Rehabilitation (PFOS)
- Fermain Wall Repair

Pipeline (£1m):

- CCTV Replacement
- Coastal Flood Defences
- Guernsey Airport Runway Infrastructure
- Home Affairs Estate Rationalisation
- Community Hub (Health and Social Care)
- HSC Digital Roadmap
- Future Guernsey Dairy
- Future Harbour Requirements
- Our Hospital Modernisation – Pathology
- SAP Roadmap
- Future Inert Waste Facility
- Our Hospital Modernisation Phase 2 and associated works
- Transforming Education Programme
- Bus Fleet Replacement Phase 3
- SMART Court Phases 2 & 3

4) Transformation projects with an estimated cost of £14m to end of 2025, including:

- Transforming Health & Social Care
- Transforming Education
- MyGov – Transforming Government Services – Next Phase

Modelling Assumptions

Key Assumption	Core	Scenario 1	Scenario 2	Scenario 3
OECD/G20 Inclusive Framework on BEPS pillar 2 - Applies minimum tax rate (15%) to companies with a global revenue of more than €750m	£10m	£10m	£10m	£10m
Other measures on corporate entities including fees and extension of 10% and 20% tax rates	£5m	£5m	£5m	£5m
Expansion or taxes on transport. Investigations including: - annual motor tax - replacement of fuel duty with distance charging - paid parking	£10m	£10m	£10m	£10m
Annual budget measures of £1m per year over 10 years including: - TRP, - document duty - excise tases, and - minor income tax changes	£10m	£10m	£10m	£10m
Investment into GWP Priorities per annum	£3m	£3m	£3m	£3m
Additional annual funding to improve IT resilience	£1m	£1m	£1m	£1m
Continuation of phased increases in Social Security contributions in their current form or a restructure of contributions raising an equivalent amount (less approx. £10m of revenue already raised)	£19m	£19m	£19m	-

APPENDIX 2

Key Assumption	Core	Scenario 1	Scenario 2	Scenario 3
Social Security Contributions restructure - allowance added for all contributors but employers aligned with Personal Income Tax Allowance (PITA) - basis changed to all income for all classes except employers - 2% rate for employers and self-employed on earnings between Upper earning limit and £250k	-	-	-	£14m
Changes to Personal income tax resulting in a loss of revenue income - increase in personal allowance by £600 - lower rate band of 15% on income up to £30k	-	-		£30m
Broad based GST with a international Services entity fee either: - 5% with tax applied on food - 6% with food zero rated	-	-	-	£75m
Cost savings	£10m	£10m	£10m	£10m
Major Capital funding (2023 to the end of the programme) *Pipeline funding included in the above* *Unforeseen Projects Provision included in the above*	£95m - -	£190m *£1m* *£0m*	£440m *£2.5m* *£12.5m*	£520m *£5m* *£31m*
Minor Capital Funding per year	£20m	£20m	£20m	£20m
Minor Capital Provision for the cost of delay	-	£4m	-	-
Incentives with social and community benefit per year	-	-	-	£2.5m
Borrowing	-	-	£200m	£350m

APPENDIX 2

Key Assumption	Core	Scenario 1	Scenario 2	Scenario 3
Use of the Health service Reserve for health-related capital expenditure	-	-	£90m	-
Use of the Health service Fund for NICE TAs (Up to an incremental cost effectiveness ratio (ICER) of £40,000)	Until end 2032 and beyond	Until end 2032 and beyond	Until end 2025	Until end 2032 and beyond

Financial Modelling Summary

Please note that the totals shown in the following tables are the sum of rounded figures, therefore apparent casting errors may appear.

Scenario 1

General Revenue only. Excludes Capital and Transformation spend.

£m	10 YEAR PROJECTIONS									
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
General Revenue Income	593	595	598	602	604	607	609	611	614	618
General Revenue Expenditure	556	568	572	574	579	585	591	597	602	607
Revenue Surplus	**38**	**27**	**26**	**29**	**25**	**22**	**18**	**15**	**12**	**11**
States Trading Assets	(4)	(3)	(2)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
Capital Income	3	1	1	1	1	1	1	1	1	1
Adjusted Operating Surplus	**37**	**25**	**25**	**29**	**25**	**22**	**18**	**15**	**12**	**11**
Brexit	(0.5)	(0.6)	(0.5)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)
Priority Actions	(1.9)	(6.1)	(5.9)	(4.0)	(3.5)	(2.9)	(2.9)	(2.9)	(2.8)	(2.8)
Revenue Impact of Capital Expenditure	(2.3)	(2.7)	(2.3)	(2.4)	(3.0)	(2.3)	(2.3)	(2.3)	(2.3)	(3.8)
Next Term's GWP	0.0	0.0	0.0	(3.0)	(3.0)	(3.0)	(3.0)	(3.0)	(3.0)	(3.0)
IT resilience costs	(1.0)	(1.6)	(2.0)	(2.5)	(2.8)	(2.9)	(2.9)	(2.9)	(2.9)	(2.9)
Savings Target	0.0	2.5	4.0	5.5	7.0	8.5	10.0	10.0	10.0	10.0
Incentives with Social/Community Benefit	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Budget income measures	0.0	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0
Tax Measures	0.0	0.0	10.0	25.0	25.0	25.0	25.0	25.0	25.0	25.0
Inflation	0.0	0.6	1.8	4.4	5.6	7.0	8.1	9.0	10.0	11.0
Operating Surplus before Financing Activities	**31**	**18**	**32**	**54**	**54**	**56**	**56**	**54**	**54**	**53**
Net Investment Return	30	28	26	25	25	24	23	22	21	19
Bond Borrowing	(4)	(6)	(6)	(6)	(6)	(5)	(5)	(5)	(5)	(4)
New Borrowing Costs	0	0	0	0	0	0	0	0	0	0
Operating Surplus after Financing Activities	**56**	**40**	**52**	**74**	**74**	**75**	**74**	**71**	**70**	**68**

APPENDIX 3

Scenario 2

General Revenue only. Excludes Capital and Transformation spend.

£m	10 YEAR PROJECTIONS									
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
General Revenue Income	593	595	598	602	604	607	609	611	614	618
General Revenue Expenditure	556	568	572	574	579	585	591	597	602	607
Revenue Surplus	**38**	**27**	**26**	**29**	**25**	**22**	**18**	**15**	**12**	**11**
States Trading Assets	(4)	(3)	(2)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
Capital Income	3	1	1	1	1	1	1	1	1	1
Adjusted Operating Surplus	**37**	**25**	**25**	**29**	**25**	**22**	**18**	**15**	**12**	**11**
Brexit	(0.5)	(0.6)	(0.5)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)
Priority Actions	(1.9)	(6.1)	(5.9)	(4.0)	(3.5)	(2.9)	(2.9)	(2.9)	(2.8)	(2.8)
Revenue Impact of Capital Expenditure	(2.3)	(2.7)	(2.3)	(2.5)	(6.0)	(3.5)	(2.1)	(2.1)	(2.1)	(2.1)
Next Term's GWP	0.0	0.0	0.0	(3.0)	(3.0)	(3.0)	(3.0)	(3.0)	(3.0)	(3.0)
IT resilience costs	(1.0)	(1.6)	(2.0)	(2.5)	(2.8)	(2.9)	(2.9)	(2.9)	(2.9)	(2.9)
Savings Target	0.0	2.5	4.0	5.5	7.0	8.5	10.0	10.0	10.0	10.0
Incentives with Social/Community Benefit	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Budget income measures	0.0	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0
Tax Measures	0.0	0.0	10.0	25.0	25.0	25.0	25.0	25.0	25.0	25.0
Inflation	0.0	0.6	1.8	4.4	5.2	6.8	8.2	9.0	10.1	11.4
Operating Surplus before Financing Activities	**31**	**18**	**32**	**54**	**51**	**55**	**56**	**54**	**54**	**55**
Net Investment Return	29	29	27	26	24	23	21	19	17	15
Bond Borrowing	(4)	(6)	(6)	(6)	(6)	(5)	(5)	(5)	(5)	(4)
New Borrowing Costs	0	(4)	(9)	(11)	(11)	(11)	(11)	(11)	(10)	(10)
Operating Surplus after Financing Activities	**56**	**37**	**44**	**63**	**59**	**61**	**61**	**58**	**56**	**55**

Scenario 3

General Revenue only. Excludes Capital and Transformation spend.

£m	10 YEAR PROJECTIONS									
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
General Revenue Income	593	595	598	602	604	607	609	611	614	618
General Revenue Expenditure	556	568	572	574	579	585	591	597	602	607
Revenue Surplus	**38**	**27**	**26**	**29**	**25**	**22**	**18**	**15**	**12**	**11**
States Trading Assets	(4)	(3)	(2)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
Capital Income	3	1	1	1	1	1	1	1	1	1
Adjusted Operating Surplus	**37**	**25**	**25**	**29**	**25**	**22**	**18**	**15**	**12**	**11**
Brexit	(0.5)	(0.6)	(0.5)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)
Priority Actions	(1.9)	(6.1)	(5.9)	(4.0)	(3.5)	(2.9)	(2.9)	(2.9)	(2.8)	(2.8)
Revenue Impact of Capital Expenditure	(2.3)	(2.8)	(2.8)	(3.2)	(5.5)	(2.7)	(2.3)	(2.3)	(2.3)	(2.3)
Next Term's GWP	0.0	0.0	0.0	(3.0)	(3.0)	(3.0)	(3.0)	(3.0)	(3.0)	(3.0)
IT resilience costs	(1.0)	(1.6)	(2.0)	(2.5)	(2.8)	(2.9)	(2.9)	(2.9)	(2.9)	(2.9)
Savings Target	0.0	2.5	4.0	5.5	7.0	8.5	10.0	10.0	10.0	10.0
Incentives with Social/Community Benefit	0.0	(2.5)	(2.5)	(2.5)	(2.5)	(2.5)	(2.5)	(2.5)	(2.5)	(2.5)
Budget income measures	0.0	1.0	2.0	3.0	4.0	5.0	6.0	7.0	8.0	9.0
Tax Measures	0.0	0.0	10.0	60.7	68.6	66.0	63.3	60.5	57.8	58.3
Inflation	0.0	0.5	1.6	7.2	10.0	12.4	14.2	15.6	17.0	19.4
Operating Surplus before Financing Activities	**31**	**15**	**28**	**90**	**97**	**99**	**98**	**94**	**91**	**94**
Net Investment Return	29	28	30	31	32	32	32	33	32	32
Bond Borrowing	(4)	(6)	(6)	(6)	(6)	(5)	(5)	(5)	(5)	(4)
New Borrowing Costs	0	(4)	(13)	(19)	(19)	(19)	(18)	(18)	(18)	(17)
Operating Surplus after Financing Activities	**56**	**34**	**39**	**96**	**105**	**107**	**106**	**103**	**101**	**104**

Glossary of Terms

Assumptions	Informed set of statements that dictate the forecast figures in a financial model
Baseline	Shows the projected financial position of continuing "as is", or could refer to the current scheme categorisation in the capital portfolio (delivery or pipeline)
Bridge-to-Bond	Where a bank facility, such as a Revolving Credit Facility, is utilised to fund cashflows until the facility reaches a certain size. When appropriate and once debt reaches a certain level, the bank facility can be converted into a bond. This financing strategy is thought to best meet the objectives of flexibility, while minimising funding costs and attaining funding security
Capital Investment	The purchase or development of capital assets e.g., buildings and infrastructure
Capital Portfolio	Group of major capital projects prioritised in line with the States strategic objectives
Contributory Funds/Social Security Funds	Incorporates the Guernsey Insurance Fund, Guernsey Health Service Fund (GHSF) (pre-2022), and the Long-Term Care Insurance Fund. The GHSF was ring fenced and retained within the General Revenue Reserve as the Guernsey Health Reserve (GHR) from 1st January 2022.
Core Investment Reserve	The only long-term reserve, the capital value is only available to be used in the exceptional and specific circumstances of severe and structural decline or major emergencies.
Depreciation	Refers to an accounting method used to allocate the cost of a tangible, or physical, asset over its useful life.
The Funding & Investment Plan (F&I Plan)	This is the Governments medium term financial plan (MTFP). It addresses how the priorities of the Government including the GWP and schemes within the capital portfolio should be funded and financed.
Fiscal Policy Framework	Set of rules agreed by Government governing tax rates and public spending. They commit the States to a guiding principle of permanent balance meaning in the long-term the States should not spend more money than it receives in taxes and other sources of income.

General Revenue Reserve	Also referred to as the 'General Reserve'. This reserve is used to fund all of the States General Revenue expenditure, including all capital, transformational and GWP initiatives.
GDP	Gross Domestic Product (GDP) is a measure of the size of an economy. In Guernsey this is calculated as the sum of compensation of employees (such as wages and pension contributions), gross operating surplus (such as company trading profits), remuneration and profits of sole traders and the income of households.
GST	Goods and Services Tax (GST) is a type of tax levied on most goods and services sold for domestic consumption.
Guernsey Insurance Fund (GIF)	The Guernsey Insurance Fund (GIF) is the fund accumulated from the schemes surpluses and is used as a buffer fund to smooth years of deficit. The associated schemes provide financial assistance during old age, bereavement, incapacity, unemployment, maternity /early parenthood and death.
GVA	Gross Value Added (GVA) is a measure of how much each sector contributes to Gross Domestic Product.
GWP	The Government Work Plan (GWP) is the framework that sets out the prioritised work for the States political term (2021 – 2025), linking it to the resources available both in terms of funding and people.
Health Service Reserve (HSR)	The Health Service Reserve is used to support the long-term sustainable provision of health and social care services, manage unanticipated health spending pressures on an in-year basis and to manage demographic pressure on the provision of these services.
Inflation	Represents the rate of increase in prices over a given period of time (most commonly a year).
Investment Returns	A gain or loss as a result of investments which can vary significantly.
Interest Rates	Interest is the monetary charge for borrowing money, generally expressed as a percentage.
Liquid Assets	A type of asset that can be rapidly converted into cash while keeping its market value.
Long Term Care Insurance Fund (LTCIF)	The Long-Term Care Insurance Fund (LTCIF) is the fund accumulated from the schemes surpluses and is used as a buffer fund to smooth years of deficit. The associated schemes are designed to assist with the

	cost of providing care in private nursing and residential homes.
Major Capital	Large capital projects, such as the building of a school, or any significant capital expenditure over £2m.
Minor Capital Expenditure	The purchase of low-value capital goods, such as police cars and IT infrastructure up to a maximum value of £2m.
NICE TAs	National Institute for Health and Care Excellence (NICE) technology appraisals (TAs) are recommendations on the use of new and existing drugs and treatments within the NHS.
Nominal Prices	The current, face value price of a good or service in monetary terms without taking account of inflation.
Operating surplus/deficit	Defined as revenue income less revenue expenditure
Overall Funding Requirement	The overall funding required by the States to deliver services, taking into account capital expenditure, the Social Security funds income and expenditure and the net impact of financing activities.
Overall Surplus/Deficit	Defined as revenue income less revenue expenditure less capital spend. Under accounting rules capital spend would be replaced with depreciation, however, this F&I Plan is focused on understanding the cash required to deliver government priorities.
Pipeline	The pipeline contains schemes requiring development work and likely to commence after this political term. The purpose of including pipeline schemes is to seek to extend the planning horizons and ensure that schemes are ready to commence detailed planning work/delivery in the next portfolio period, subject to prioritisation. Those schemes identified as pipeline can access funding to commence preliminary work to provide clarity in terms of direction and scope.
Principal Committees	‘Principal Committees’ in this policy letter refers to engagement with the following groups: Policy & Resources Health & Social Care Education, Sport & Culture Environment & Infrastructure Economic Development Employment & Social Security Home Affairs States’ Trading Supervisory Board Development & Planning Authority

Private Placement	A private placement is similar to a public bond in terms of being a longer dated financial instrument, however, it will likely have restrictions more similar to a bank facility.
Public Sector	The governance, services and infrastructure owned and operated by the Government.
Real Prices	The price for goods or services relative over time including inflation.
Revenue Surplus/Deficit	Revenue deficit can be calculated by taking the total revenue expenditure and subtracting it from revenue income.
Structural Deficit	A structural deficit is defined as a government deficit that is independent of the business cycle and is created when a government is spending more than the long-term average tax revenues it is receiving.

RICE	Revenue impact of capital expenditure (RICE) is the revenue cost associated with capital projects, for example the cost of a service contract for a piece of equipment.
RPI	Retail Prices Index – a measure of the price inflation experienced by people living in private households on all items (including mortgage interest payments)
RPIX	Retail Prices Index – a measure of the price inflation experienced by people living in private households on all items (excluding mortgage interest payments)
SLAWS	Supported Living and Ageing Well Strategy
Social Security Deficit	The difference between the income raised through contributions which is retained by the funds and the cost of demand for services.
Strategic Portfolio	The strategic priority workstreams as defined in the Government Workplan
Structural Deficit	A government deficit that is independent of the business cycle and is created when a government is spending more than the long-term average tax revenues it is receiving

Portfolio on a Page

PORTFOLIO 1				
DO AS PLANNED		**DO BUT REVIEW SCOPE &/OR SOLUTION**		**PIPELINE (£1m provision included to progress schemes)**
Scheme Name	**Cost to Complete £m**	**Scheme Name**	**Cost to Complete £m**	**Scheme Name**
Property Rationalisation Phase 2	0.6	Guernsey Airport Pavements Rehabilitation (PFOS)	4.9	CCTV Replacement
Clinical & Animal Waste Solution	3.2	Fermain Wall Repair	0.4	Coastal Flood Defences
Community Services - Children & Families Hub	8.0			Guernsey Airport Runway Infrastructure
Central Stores - Supply Chain Relocation	5.0			Home Affairs Estate Rationalisation
Bridge Regeneration (Housing and SS Bridge Flood Defences)	35.0			Community Hub (Health and Social Care)
Future Harbour Requirements - Survey	4.0			HSC Digital Roadmap
Alderney Airport Pavements Rehabilitation	23.7			Future Guernsey Dairy
Repair/Replacement of Castle Emplacement Bridge	6.7			Future Harbour Requirements
				Our Hospital Modernisation - Pathology
				SAP Roadmap
				Future Inert Waste Facility
				Our Hospital Modernisation Phase 2 and associated works
				Transforming Education Programme
				Bus Fleet Replacement Phase 3
				SMART Court Phases 2 & 3

PORTFOLIO 2				
DO AS PLANNED		**DO BUT REVIEW SCOPE &/OR SOLUTION**		**PIPELINE (£2.5m provision included to progress schemes)**
Scheme Name	**Cost to Complete £m**	**Scheme Name**	**Cost to Complete £m**	**Scheme Name**
Property Rationalisation Phase 2	0.6	Guernsey Airport Pavements Rehabilitation (PFOS)	4.9	CCTV Replacement
Clinical & Animal Waste Solution	3.2	Fermain Wall Repair	0.4	Coastal Flood Defences
Community Services Children & Families Hub	8.0	Bus Fleet Replacement Phase 3	2.5	Guernsey Airport Runway Infrastructure
Central Stores - Supply Chain Relocation	5.0	SMART Court Phases 2 & 3	2.5	Home Affairs Estate Rationalisation
Bridge Regeneration (Housing and SS Bridge Flood Defences)	35.0			Community Hub (Health and Social Care)
Future Harbour Requirements - Survey	4.0			HSC Digital Roadmap
Alderney Airport Pavements Rehabilitation	23.7			Future Guernsey Dairy
Repair/Replacement of Castle Emplacement Bridge	6.7			Future Harbour Requirements
Our Hospital Modernisation Phase 2 and associated works	120.0			Our Hospital Modernisation - Pathology
Transforming Education Programme	119.3			SAP Roadmap
				Future Inert Waste Facility

APPENDIX 5

PORTFOLIO 3				
DO AS PLANNED		**DO BUT REVIEW SCOPE &/OR SOLUTION**		**PIPELINE (£5m provision included to progress schemes)**
Scheme Name	**Cost to Complete £m**	**Scheme Name**	**Cost to Complete £m**	**Scheme Name**
Property Rationalisation Phase 2	0.6	Guernsey Airport Pavements Rehabilitation (PFOS)	5.0	CCTV Replacement
Clinical & Animal Waste Solution	3.0	Fermain Wall Repair	0.4	Coastal Flood Defences
Community Services Children & Families Hub	8.0	Bus Fleet Replacement Phase 3	2.5	Guernsey Airport Runway Infrastructure
Central Stores - Supply Chain Relocation	5.0	SMART Court Phases 2 & 3	2.5	Home Affairs Estate Rationalisation
Bridge Regeneration (Housing and SS Bridge Flood Defences)	35.0			Community Hub (Health and Social Care)
Future Harbour Requirements - Survey	4.0			HSC Digital Roadmap
Alderney Airport Pavements Rehabilitation	24.0			Future Guernsey Dairy
Repair/Replacement of Castle Emplacement Bridge	7.0			Future Harbour Requirements
Our Hospital Modernisation Phase 2 and associated works	120.0			Our Hospital Modernisation - Pathology
Transforming Education Programme	119.0			
SAP Roadmap	25.0			
Future Inert Waste Facility	35.0			

Fiscal Policy Framework

The Fiscal Policy Framework, first established in 2009, sets out the island's highest level of fiscal policy, including the boundaries within which more detailed fiscal policy should operate. The Framework provides a series of high-level principles which commit the States to an overarching theme of long-term permanent balance (not spending more than is received) and ongoing fiscal prudence. These principles define fiscal boundaries in terms of long-term fiscal balance and include limits on revenues, deficits and debt against which the States can be monitored and held accountable. It is designed to endure across multiple political terms to promote stability and consistency in fiscal policy.

The framework was last reviewed by the States of Deliberation in 2020[1] and a summary of the agreed framework is provided below.

Principle 1: Guernsey's fiscal policy should operate on a principle of long-term permanent balance.

This has been the governing principle of the Framework since its introduction and all subsequent principles stem from this. It means that, over the long-term, Guernsey should not spend more money on public services than it receives in revenues.

Long-term balance is about more than just balancing the Annual Budget. It is about managing the States' resources in the long-term to ensure fiscal sustainability. This principle is be supported with indicators which monitor:

- The value of the Core Investment Reserve, recognising that the value of these assets should be increased over time in line with the current policy of targeting one year's revenues as the balance of the Reserve (as approved in the Medium-Term Financial Plan 2017-2021).
- The long-term projections of the Guernsey Insurance Fund and the Guernsey Long Term Care Fund, recognising the planned drawdown of these funds to support demographic change and the aim to maintain these reserves with at least two years of expenditure (as referenced in the Personal Tax, Pensions and Benefits Review (Billet d'État IV, March 2015).

Principle 2: The annual net deficit reported on the General Revenue accounts for any given year should not exceed 15% of operating revenues.

This principle sets out the maximum value of any deficit the States might have in any given year.

[1] Billet d'État I 2020

This principle is to govern the net deficit, defined as operating surplus/deficit plus investment returns, capital receipts, finance charges and capital spending (to be replaced with depreciation under IPSAS).

Principle 3: Annual net deficits reported in the General Revenue accounts should not be allowed to persist for more than five consecutive years.

This principle recognises that, as well as limiting the size of deficits it is necessary to limit the length of time over which they can persist. Even relatively modest deficits can drain resources if allowed to persist over time.

Under the principle of long-term permanent balance, periods of deficit need to be balanced by periods of surplus to replenish reserves.

Principle 4: Measures to address any identified or anticipated deficit must be incorporated in the States Medium Term Financial Plan (MTFP).

This might include a combination of reductions in expenditure, revenue-raising measures and measures to stimulate growth appropriate to the circumstances of the deficit.

The intention of this principle is to require a formal response to a deficit, without pre-determining the most appropriate response.

The MTFP was previously produced every four years and included forecasts of the expected financial position over the four-year period. This has now been replaced by the Funding and Investment Plan (F&I Plan).

Principle 5: The aggregate amount of States' revenue should not exceed 24% of GDP.

This includes all forms of taxation from within General Revenue, Social Security contributions and the operating income of committees, but does not include the return on investments.

This principle governs the aggregate size of the public sector in Guernsey. Its intention is to provide a limit on the maximum amount of money it is deemed appropriate to take out of the general economy to be redirected to the provision of public services. With the exclusion of investment income, government revenue is generated from taxes and charges levied on local residents and businesses and Guernsey's status as a low tax jurisdiction is an important part of its competitive position as a finance centre.

Principle 6: Total capital expenditure over any States term should be maintained at a level which reflects the need for long and medium term investment in infrastructure and direct capital expenditure by the States should average no less than 1.5% of GDP per year averaged over a four-year period and 2% per year averaged over any eight-year period.

This should be identified through the infrastructure plan and the medium term capital plan. The MTFP should ensure sufficient resources are allocated to deliver on these requirements.

Direct capital expenditure includes any capital spending supported with recourse to general taxation or reserves.

Principle 7: The States' total debt should not exceed 15% of GDP.

Gross debt can be deployed only to finance the investment in infrastructure or assets. Any project or acquisition supported with recourse to government debt must be able to generate sufficient revenue to meet the repayment of that debt.

The definition of debt includes any direct borrowing and contingent liabilities associated with guaranteeing the borrowing of States trading entities, States owned enterprises and Non-Government Organisations (NGOs).

Guarantees or assurances offered on the operational cash flow arrangements of the States trading entities and states owned enterprises (for example the guarantee of overdraft facilities) are excluded.

Under this principle government debt can only be used to buy, develop or improve assets which have both a community and commercial value. It also allows for the fact that these assets may not necessarily be directly owned by government.

Capital Portfolio - Scheme Descriptions

The table below provides a brief description of all schemes currently included within the capital portfolio (in alphabetical order).

	Scheme Name	Description
1	Alderney Airport Runway Rehabilitation	Option C+ - A full refurbishment of the existing aerodrome pavements, runway and apron to accommodate Code C aircraft together with a new terminal building and a refurbished and reconstructed fire station.
2	Bridge Regeneration (Housing and SS Bridge Flood Defences)	Project for housing units and to provide sufficient protection from the risk of overtopping at St Sampson's Harbour.
3	Bus Fleet Replacement (Phase 3)	Final phase of a 2 Phased programme of bus fleet replacement: the purchase of 8 replacement vehicles
4	CCTV Replacement	To review the scope and requirements for a multi-agency CCTV capability to meet current and future demands of crime prevention & detection, to ensure enhanced community safety and enhance the security of the Bailiwick's Critical National Infrastructure.
5	Central Stores - Supply Chain Relocation	An enabler to achieve operational and revenue efficiencies and critical enabler required ahead of any future redesign of the Princess Elizabeth Hospital (OHM Phase 2).
6	Clinical & Animal Waste Solution	The replacement of both Clinical Waste and Animal Carcass Incinerators with a solution at a combined site at the Longue Hougue Waste Facility.

	Scheme Name	Description
7	Coastal Flood Defences	To review and scope the flood mitigation measures at St Sampson harbour (the Bridge) and Belle Greve Bay. (Note that "phase 2" is the investigation into and provision of flood mitigation at Belle Greve).
8	Community Services - Children & Family Services Hub	Recognising the benefit of early intervention and wrap-around services for families, the operational importance of co-locating States services alongside securing capital receipts by vacating, and then disposing of several buildings.
9	Community HUB (Health and Social Care)	To review and scope the optimum solution for HSC community-based services.
10	Fermain Bay Repair	Addressing the coastal path at Fermain Bay.
11	Future Guernsey Dairy	To scope the facility requirements for a new dairy in order to support sustainability of the local dairy farming industry.
12	Future Harbour Requirements - Survey	Recognises the States' recent Resolution following consideration of the East Coast Development[1] and the pressing need to finalise plans for the lifeline harbours through which the Bailiwick's essential commodities are transported.
13	Future Harbour Requirements	To deliver the scope of future harbour requirements.
14	Future Inert Waste Facility	To scope, plan and implement a future inert waste disposal facility.

[1] Billet d'État X of 2023, Article 14

	Scheme Name	Description
15	Guernsey Airport Pavements Rehabilitation (PFOS Contingency)	To scope, plan and implement a solution to transfer the contaminated soils to the selected processing plant in the UK or Europe.
16	Guernsey Airport Runway Infrastructure	To scope and conclude the requirements and benefits of an extended runway
17	Guernsey Tourism Product Development	To develop the Tourism Plan and consider areas of investing in visitor attractions, Scheme deprioritised.
18	Home Affairs Estate Rationalisation	To scope for the rationalisation of the Home Affairs estates to meet the demands of the in-scope services.
19	HSC Digital Roadmap	To scope the future use of digital technology in HSC.
20	Our Hospital Modernisation Programme Phase 2 and associated works	The refurbishment of theatres, sterile services, orthopaedic ward, breast unit, fracture clinic and private ward, delivery of a new emergency department and outpatients, works to plant room and other areas. New Build also includes maternity, neonatal intensive care unit, paediatric ward, admissions/discharge unit, outpatients, main entrance, additional theatres.
21	Our Hospital Modernisation Pathology	States of Guernsey laboratory operations include analytical, chemical, micro-biological, clinical & pathological, and horticultural services. The aim of this project is to rationalise and modernise these laboratory services.
22	Property Rationalisation	Phase 2 of the property rationalisation programme which includes the relinquishment, leasing or re-purposing of buildings by the States Property Unit including:

	Scheme Name	Description
		• Raymond Falla House • Bulwer Avenue • Old Tobacco Factory • New Jetty • New ways of working and staff moves have also been carried out with a focus on 2 main civic buildings at Edward T Wheadon House and Sir Charles Frossard House
23	Repair / Replacement of Castle Emplacement Bridge	To repair or replace the existing concrete bridge which connects Castle Breakwater, Castle Cornet, and Castle Emplacement.
24	SAP Roadmap	To scope, plan design and deliver the replacement of the Enterprise Resource Platform.
25	SMART Court Phases 2 & 3	Aimed at enabling more efficient services to be provided from the Greffe, HM Sheriff and Sergeant, and Registrations departments through digital and information technologies.
26	Territorial Seas & Fisheries Enforcement	To review and make the most cost-effective provision of a States' fisheries patrol and enforcement capability – which is also capable of wider use for other States marine tasks. Scheme deprioritised.
27	Transforming Education Digital – The Guernsey Institute	Remaining elements of the Education Digital project relating to The Guernsey Institute at its future location at Les Ozouets Campus.
28	Transforming Education Programme – construction elements	Creation of a new education campus at Les Ozouets, for all forms of post-16 education as well as other capital works required across the secondary education estate.

In-Flight and Delivered Schemes

The States have made progress in the advancement of the current portfolio (2021 to 2024) including some legacy projects. Since 2021, the following schemes have been delivered and / or are in-flight. The table below provides a brief description of these schemes (in alphabetical order).

	Scheme Name	Description
1	Bus Fleet Replacement – Phases 1 & 2	The planned replacement of existing ageing bus fleet.
2	Digital Infrastructure	Investing in the Guernsey digital economy through fibre connectivity.
3	EIA – Land Reclamation and Development for Inert Waste	Completion of the detailed environmental impact assessment (EIA) on potential land reclamation and future development east of the QEII marina, to help inform the preparation of the local development strategy for the St Peter Port Harbour Action Area.
4	Electronic Patient Record	Replacement of the Electronic Patient Record system.
5	Footes Lane Refurbishment	Resurfacing of the athletics track and stand refurbishment to include: • conversion to 8 lane 400 metre track; • Installation of infield drainage and artificial grass. • Maintenance and repair work to the Garenne Stand; and • Installation of multi-use accessible viewing platform and reconfiguration of toilets
6	Funding Affordable Housing Developments Programme	To supply housing units to meet the Island's affordable housing requirements. This development / redevelopment programme includes the following affordable housing tenures:

	Scheme Name	Description
		a. Social rental b. Partial ownership c. Key Worker d. Emergency Housing Provision e. Extra Care f. HSC user accommodation
7	Guernsey Airport Baggage Handling System Upgrade – Stage 1	Upgrades the existing hold baggage system including ‘in gauge and out of gauge’ x-ray machines to comply with Department for Transport security requirements.
8	Guernsey Registry IT Systems Replacement	The replacement of the bespoke registry systems that host the registers for Companies, LP's LLP's Foundations, Beneficial Ownership, and Intellectual Property.
9	Havelet Slipway Repairs	Repair of the Havelet Slipway located at the eastern end of the Castle Emplacement.
10	IT Transformation	Provide the States with IT services which will provide a stable, secure, and resilient foundation platform for Smart Guernsey (FDS) delivery, Public Service Reform (PSR) and for States staff to work and interact using a modern workplace.
11	Mont Crevelt Breakwater Reinstatement	To fill the gap in the breakwater which was created as part of the St Sampson’s Harbour Development works and to prevent material outflow.
12	MyGOV Programme	To introduce new technology to support the re-design of services and their supporting processes and manage the transition to a new model of service delivery.

	Scheme Name	Description
13	Online Passport & Workflow System	To ensures the Bailiwick can retain the ability to process and issue Island variant passports in the future by replacing the current system which exists on a non-supported platform nearing end of life and moves the Bailiwick into HM Passport Offices new fully digital environment.
14	Our Hospital Modernisation (Phase 1)	The delivery of a CCU, Post Anaesthetic Care Unit (PACU), associated staff and visitor facilities, infrastructure (electricity/oxygen distribution), and external works to support the delivery of subsequent phases.
15	Radiology Equipment Replacement	The planned Replacement of the of HSC's ageing radiology equipment.
16	Replacement Cremator	Replacement of the Islands' cremator and emissions equipment.
17	Sarnia Cherie BWMS	Installation of a ballast water management system (BWMS) on the Sarnia Cherie.
18	SMART Court Phase 1	First of three phases that are to deliver core services through digital and information technologies building digital capability to deliver an end-to-end user experience that makes use of the States' current and planned investment in technology, specifically as it affects citizen & professional contact with key services.
19	St Sampson Fire Main Pump Replacement	Replacement of the St Sampson Fire Main Pump.
20	Tetra PSN	To upgrade/replace the public safety network (PSN) and emergency services networks (ESN).

	Scheme Name	Description
21	Transforming Education Digital - secondary and primary[2]	An integral part of the Transforming Education Programme. Modernisation of the digital equipment and infrastructure used in the provision of education.
22	Transforming Revenue Service Programme	To deliver a new operating model for the collection of income tax and social security contributions through three phases.
23	Virtual Machine Environment (VME) Replacement	To replace the VME Operating System and associated applications to hold the core Revenue Service tax and contribution data.

[2] *This does not include the digital elements of the TGI Programme – this is included in the overall Transforming Education Programme*