

Financial Strategy 2018/19 to 2021/22

Report by Gary Fairley, Head of Finance and Integrated Service Support

1 Purpose of Report

This report provides Council with an update on the Financial Strategy encompassing the years 2018/19 to 2021/22.

It includes:-

- An assessment of future years Scottish Government Grant;
- Updated budget projections for 2018/19 to 2021/22;
- A sensitivity analysis reflecting the potential impact of different pay and grant settlement scenarios years;
- Details of the arrangements for the delegation of resources to the Midlothian Integration Joint Board;
- An update on the Change Programme aimed at addressing the projected budget shortfalls;
- Initial feedback from the budget engagement activity;
- An update on Reserves.

2 Background

The core objective of the Financial Strategy is that of securing the Council's continued financial sustainability during an ongoing period of substantial financial constraint coupled with continuing service demand pressures and increasing customer expectations.

The last Financial Strategy report was presented to Council on 10 October 2017 and provided an updated assessment of projected budgets shortfalls through to 2021/22. At that meeting Council agreed to proceed to engage with the community on the budget and change programme through Shaping our Future, the consultation strand of the Delivering Excellence framework.

This report provides Council with an update on the Financial Strategy, including the engagement activity, as part of the agreed process and timetable to enable Council to determine Council Tax and set a balanced budget for 2018/19 on 13 February 2018.

3 Scottish Government Grant Settlement

The Scottish Government's grant settlement is one of the most critical aspects of the financial projections in this report.

The first main development since the last report on 10 October 2017 was the publication of the UK Government's autumn budget on 22 November 2017 along with the latest Office for Budget Responsibility Economic and Fiscal Outlook. This contained spending plans for all UK departments and devolved administrations through to 2019/20 for resource spending and 2020/21 for capital spending as well as a range of tax plans in advance of the new tax year in April 2018.

SPICe, The Scottish Parliament Information Centre, has published a briefing Paper, "UK Autumn Budget 2017 - Impact on Scotland" (1) which summarises the implications of that budget for Scottish public finances. It identifies that overall, the resource budget element of the Scottish block grant will increase in cash terms in 2018/19 by 0.7% which represents a real terms fall of 0.8%. The capital element will see a cash increase of 7.8% next year, equivalent to a 6.2% increase when adjusted for inflation.

- 1) [SPICe, The Scottish Parliament Information Centre, Briefing Paper, "UK Autumn Budget 2017 - Impact on Scotland"](#)

£0.5 billion of the Barnett consequential over the period of the budget relates to extra NHS related spend (both capital and revenue) and if, as has typically happened in the past, this is ring-fenced for the NHS in Scotland there may be little of the additional funding left to be distributed amongst other budgets, especially Local Government.

Until recently, Scottish Governments resources came almost exclusively via the block grant from the UK Government. The devolution of further tax powers in the Scotland Act 2016 means that decisions made in Scotland will now have greater influence over the size of the Scottish budget. In 2018/19 it is estimated that around 30% of the Scottish Government's budget will come from income tax receipts in Scotland and a further 7% will come from other taxes determined by the Scottish Parliament.

On 2 November 2017 the Scottish Government published "The Role of Income Tax in Scotland's Budget". The stated aim of this report is that of supporting a debate about the financing of public services in preparation for setting Scotland's budget for 2018/19. The report sets out a number of approaches which could be considered and which it is estimated would raise between £82 and £255 million per annum to support the Scottish Government's £39 billion budget.

The Scottish Government had already indicated that its future pay policy would take account of the cost of living, thereby removing the 1% pay cap. The consumer price index (CPI) is currently 2.8% and at this point it remains unclear what, if any, additional resources Government may provide to Local Authorities to support increases in their pay bill which take account of the cost of living. The Council's Financial Strategy makes provision for pay awards of 1.5% per annum, with the assumption that the cost of awards above this would only be deliverable if they were supported by funding through the grant settlement. Council should note that to uprate the provision for pay awards to the level of CPI, without any additional funding, would

further increase the budget shortfall in 2018/19 by £1.350 million rising to over £5.500 million by 2021/22.

In advance of the UK Government budget and COSLA launched a 10-page factual document entitled “Fair Funding for Essential Services” (2) laying out the case for a fair settlement for local government. The document highlights that for 2018/19 local government needs:-

Revenue Settlement

1. *No more cuts - parity with cash increase for Scottish Government.*
2. *Full baselining of £130m funding from the 2016-17 budget agreement.*
3. *Allow for proper investment in the local government workforce.*
 Every 1% on local government paybill costs £70m
 Every 10p increase in living wage for adult social care providers costs £10m.
4. *Additional investment in Health and Social Care in recognition of the rising demand.*

Structure of Settlement

1. *Multi-year budgets.*
2. *Create flexibility to help deal with pressures.*

We cannot continue with 58% of the budget being nationally ring-fenced. We need true removal of ring-fencing and central direction through input targets.

Capital

1. *Increased capital funding to invest in and attract growth.*
2. *Return of reprofiled capital funding.*

Local Taxation

1. *Removal of the 3% cap on Council Tax.*
2. *Proper reform of local taxation.*
3. *Power to introduce discretionary taxation.*

Funding for Government Policies

1. *Full and transparent funding for new central government initiatives.*
 Specifically:
 Expansion of early learning and childcare
 Living wage for adult health and social care workers
 Carers Act
 2. *If charitable status of ALEOs is withdrawn, then the £45m shortfall in delivery of these services needs to be met.*
- (2) [COSLA - Fair Funding for Essential Services](#)

The Cabinet Secretary for Finance and the Constitution will publish the Scottish Government’s one year budget and income tax proposals for 2018/19 on 14 December 2017. The Finance Circular setting out the proposed individual Council grant settlements figures and associated conditions, again for 2018/19 only, is expected to be published alongside the budget. Council will be provided with a verbal update based on the initial analysis of the budget and grant settlement.

Thereafter the parliamentary process for approving Government’s budget is expected to be concluded in early February 2018. Members may recollect that for 2017/18 changes made during the parliamentary process resulted in an additional provision in the grant settlement for Local Government from that originally published in December 2016.

In summary the key factors which influence the level of grant support Council might expect for 2018/19 and beyond are, firstly a range of economic factors will influence the resources Governments have at their disposal, whether from the UK Government or through tax revenues directly controlled by Scottish Government. Others factors include the taxation and spending priorities of Scottish Government, including the extent to which it intends to support increases in public sector pay. Whilst an assessment of the economic factors can be made based on the information available from the Office of Budget Responsibility and the UK Government's spending plans the impact of Scottish Government's tax and spending priorities will only become fully apparent when the budget is published on 14 December 2017.

The latest assessment by the economic advisor engaged by the CIPFA Directors of Finance section continues to indicate that there will be a cash reduction for the "unprotected" elements of the Scottish Government budgets of which the Local Government grant is the largest element. As such the indications remain that the future years grant settlements will remain challenging with year on year cash reductions, other than for any additional resources provided to fund the cost of new legislative burdens and or specific cost pressures. It is also expected that specific conditions and direction of resources will be an increasing feature of future years grant settlements.

The central planning assumption adopted for the Scottish Government grant projections continues to be based on reductions in grant at a similar level to the original proposed 2017/18 settlement. That is an average 3.25% per annum cash reduction at a national level (against the final 2017/18 settlement, i.e. including the £130 million), offset by the impact of the relative growth in the Midlothian population. It is also assumed that Government will continue to:-

- Direct resources to Integrated Health and Social Care Boards via the NHS;
- Direct resources to Schools through the Pupil Equity Fund or equivalent;
- Provide flexibility to increase Council Tax but only by a maximum of 3%;
- Continue to set specific requirements to maintain the overall pupil/teacher ratio and secure places for all probationers who require one under the teacher induction scheme.

It is stressed that the grant settlement figures through to 2021/22 as set out table 1 are projections, the actual figures being dependant on future budget decisions taken by Scottish Government. However they do provide Council with an assessment of the impact of the grant settlement on the Council's financial position. Critically they highlight the severity of the challenge ahead for the term of this Council and the extent to which service provision will have to be significantly transformed and/or reduced.

4 Council Tax

The budget shortfalls set out in table 1 are based on the current band D Council Tax of £1,246 and reflect the additional income from an increase in the number of properties.

As indicated earlier it is assumed that grant settlement conditions will provide flexibility to increase Council Tax by up to 3%. For Midlothian a 3% per annum increase is estimated to generate £1.274 million for 2018/19 rising to £1.334 million in 2021/22 and would result in band D Council Tax rising to £1,283 in 2017/18 and to £1,403 by 2021/22.

Given the grant prospects set out in section 3 of this report the Financial Strategy incorporates the full 3% increase for each year to contribute to reducing the projected budget shortfalls.

5 Cost of Services

The projected cost of services for future years is derived from the 2017/18 approved budget. The projections have been updated to reflect the latest information available and work will continue to refine the budget projects with any further changes incorporated into the final report for 2018/19 to Council on 13 February 2018.

Table 2 provides an analysis of the principle year on year budget changes which include the following key assumptions and cost drivers:

- Pay inflation of 1.5% per annum for all staff groups together with the cost of incremental pay progression, with the assumption that any increases above this level would require additional Government funding;
- The impact of Pension Reform and anticipated changes in the Council's contribution towards employee pensions costs;
- Provision for the Devolved School Management allocation to schools based on the current scheme, indicative pupil numbers and the requirement to maintain the pupil teacher ratio;
- Contractual inflation linked to existing contractual conditions, many of which mirror pay inflation assumptions;
- A provision for the future years costs of maintain pay levels for procured care services at or above the living wage;
- The impact of current demand for services;
- A reassessment of 2017/18 savings targets to more fully reflect deliverability of these changes;
- The demographic impact on the future demand for services;
- Borrowing costs related to capital investment decisions based on future interest rate forecasts provided by the Council's Treasury Advisers;
- Any new Government policy requiring budgetary growth will be fully funded through increased Scottish Government grant;
- Council Tax income continues to grow in line with previous trends and planned future housing growth.

The updated projected budget shortfalls reflecting the assumptions set out in sections 3 to 5 are therefore as follows:-

Table 1: Budget Shortfalls 2018/19 to 2021/22 – 19 December 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Cost of Services	205.687	214.206	221.672	229.251
Less: Council Tax	(45.604)	(46.204)	(46.854)	(47.504)
Less: Scottish Government Grant	(146.002)	(142.687)	(139.443)	(136.269)
Budget Shortfalls	14.081	25.315	35.375	45.478

The budget shortfall in 2018/19 equates 7% of the net cost of services and the projections indicate this could rise to 20% by 2021/22. As Council is aware, significant elements of the budget are either fixed or are challenging to change for a number of reasons including:-

- Historic decisions, for example, loan charges and unitary charge contractual payments;
- Specific conditions, for example the maintenance of the teacher pupil ratio; and
- Growing demand for services through demographic pressures.

These elements of the budget equate to £112 million in 2018/19 and are projected to rise to £140 million by 2021/22. Consequently the budget shortfall expressed as a percentage of the remainder of the budget equates to 14% for 2018/19 and has the potential to rise to 50% by 2021/22.

Whilst the projected cost of service provision, Council Tax and Scottish Government grant has been projected forward to 2021/22 these remain indicative projections based on the assumptions set out in sections 3 to 5 and will inevitably change over the period. The projections and planning assumptions on which they are based will be updated and reported to Council as new information becomes available.

The main purpose of the future year projections is to provide Council with an assessment of the key factors which influence income and expenditure and the overall impact these may have on the Council's financial position over the medium term. Critically they highlight the severity of the challenge ahead for the term of this Council and the extent to which service provision will have to be significantly transformed and or reduced. Members should note that the projections are based on the continuation of the existing service delivery and funding arrangements.

The budget shortfalls set out in table 1 arise for the following reasons:

Table 2: Analysis of Shortfalls – 19 December 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Opening Shortfall	3.970	14.081	25.315	35.375
Pay Inflation and Salary Progression	2.493	2.944	2.947	3.101
Pension Contributions	0.450	0.450	0.450	0.000
Contractual Inflation	0.697	0.637	0.571	0.652
Demographics: Care	1.040	1.040	1.040	1.040
Demographics: School Rolls	2.260	2.770	2.798	3.083
25 Hours in Primary Schools	0.090	0.000	0.000	0.000
Demand pressures: Children	0.453	0.024	0.024	0.024
School Estate Investment	0.381	1.126	0.033	0.036
Waste Disposal Costs	0.213	(0.285)	0.125	0.125
Non Domestic Rates	0.132	0.135	0.138	1.142
Borrowing Costs	(0.003)	(0.089)	0.123	(0.007)
Scottish Government Grant	3.172	3.315	3.244	3.174
Council Tax Income	(0.600)	(0.600)	(0.650)	(0.650)
Full year effect of 2017/18 savings	(0.989)	(0.258)	(0.860)	(0.610)
Reinstatement of Community Policing Teams	0.563	0.006	0.006	0.006
Other Movements	(0.241)	0.019	0.071	(1.013)
Totals	14.081	25.315	35.375	45.478

Since the last report further work has been undertaken to assess the financial impact of current service pressures for later years and also to reflect a review of the 2017/18 savings targets. While these result in increased budget shortfalls over the four years it results a more representative assessment of the cost of current service provision. The principal movement from the figures set out in the 10 October 2017 report are as follows.

Table 3: Movement from 10 October 2017 to 19 December 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Shortfall 10 October 2017	13.495	24.629	34.689	44.792
Revised full year effect of 2017/18 savings	0.307	0.407	0.407	0.407
Net base budget pressures for Children's Services	0.129	0.129	0.129	0.129
Increase provision for utility price increases	0.150	0.150	0.150	0.150
Shortfall 19 December 2017	14.081	25.315	35.375	45.478

6 Sensitivity Analysis

Given the level of uncertainty for future year grant settlements and outstanding pay awards table 4 provides a sensitivity analysis reflecting the potential impact of different scenarios/outcomes for these two key aspects of the budget.

Scenario 1. This is a more optimistic scenario which assumes a 1.5% pay award in each of the years but with cash flat grant settlements. Otherwise all other assumptions remain as set out in section 3.

Scenario 2. Is a more pessimistic scenario which assumes a 3% pay award and reducing grant income as set out in section 2.

Table 4: Sensitivity Analysis – 19 December 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Scenario 1				
Central Assumption	14.081	25.315	35.375	45.478
Cash Flat Government Grant	(3.172)	(6.487)	(9.731)	(12.905)
Amended Shortfall	10.909	18.828	25.644	32.573
Scenario 2				
Central Assumption	14.081	25.315	35.375	45.478
Revised Pay Award Assumption	1.800	3.600	5.550	7.500
Amended Shortfall	15.881	28.915	40.925	52.978

These scenarios demonstrate the significance of the impact that changes from the central planning assumption for either government grant or pay inflation have on the projected budget shortfalls.

7 Midlothian Integration Joint Board

As part of the budget setting process the Council will need to determine an allocation of resources to the Midlothian Integrated Joint Board (IJB). For 2017/18 the allocation is £37.571 million.

The projected budget shortfalls set out earlier incorporate a provision for pay awards, inflationary uplifts and a sum for demographic cost pressures in respect of services delegated to the IJB. It does not provide for further uplifts in the Living Wage for care providers on the assumption that resources for this have been provided from the Social Care Fund. In turn the proposed Change Programme provides these cost pressures to be significantly offset. The indicative allocation of resources for 2018/19 and future years is estimated to be:-

Table 5: Indicative IJB allocation 19 December 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Previous Year's Allocation	37.571	38.086	38.611	38.136
Uplifts:				
Pay and inflation	0.515	0.525	0.525	0.525
Demographic Pressures	1.040	1.040	1.040	1.040
	39.126	39.651	40.176	39.701
Change Programme Savings	(1.040)	(1.040)	(2.040)	(1.540)
Indicative Allocations	38.086	38.611	38.136	38.161

A review is being undertaken in respect of the budget provision for client transport, estimated at £0.500 million, which does not currently form part of the resources delegated to the IJB with a view to including these resources within the delegated budget for 2018/19 onwards.

At this point it is recommended that the IJB is formally advised of the indicative allocation for 2018/19 along with the projection for later years and that discussions continue with officers of the IJB to secure sustainable strategy for the delivery of delegated services which can be delivered within the proposed resource allocation. This ongoing dialogue will inform the development of both the Council's and the IJB's Financial Strategies. A decision on the final allocation for 2018/19 will need to be made by Council on 13 February 2018.

This approach will support the IJB as it develops its own Financial Strategy within the context of the financial pressures and the available allocations anticipated to be available from both the Council and NHS Lothian.

8 Change Programme

In addition to the delivery of savings approved in the current and previous financial years, the savings targets associated with the existing transformation programme, and continued control over expenditure, the strands of work that will continue to be necessary to address the projected budget shortfalls represent an emerging Change Programme, encompassing:-

- Delivering Excellence;
- An updated and expanded programme of transformation activity;
- The EWiM programme;
- An updated Capital and Reserves Strategy;
- Operational savings encompassing financial discipline measures;
- A series of savings proposals.

8.1 Delivering Excellence

The Delivering Excellence framework supports the repositioning of services to ensure they have a greater emphasis on and achieve better outcomes for those most disadvantaged and vulnerable in the community. The framework focuses on reshaping service delivery as the most sustainable way to address the financial and service challenges and maintain financial sustainability.

The framework sets out an approach that provides the means to:

- Realise savings of the scale and magnitude required and to continue to deliver high quality services by engaging staff, partners, stakeholders and citizens to determine the nature of service delivery, the level of service standards and the method of delivering these services;
- To perform successfully in this environment, the Council will require to forward plan for the period beyond known financial settlements, to prioritise the services to be delivered and to clearly identify those services which will no longer be funded or indeed provided or may be provided through alternative mechanisms or approaches; and
- To ensure that there is achievement of the outcomes and priorities of the Council and Community Planning Partners.

Change Programme proposals were presented to Council on 10 October 2017 to facilitate a period of engagement with the community on the budget and Change Programme through shaping our future, the engagement strand of the Delivering Excellence framework. The engagement period to help inform 2018/19 decisions runs until 14 December 2017. An interim overview of feedback from the engagement activity is set out in appendix 1. It is proposed that a detailed report is prepared and made available to all members early in the New Year and that it is also considered by the Business Transformation Steering Group on 15 January 2018.

It is recognised that the proposals set out on 10 October 2017 did not fully address the 2018/19 budget shortfall projected at that time or give Council any headroom to consider options or indeed allow a contribution to Reserves. Accordingly, and also recognising the updated projections set out in this report, work is ongoing to develop further proposals and also to amend some of the existing proposals to take cognisance of the feedback from the engagement activity. It is anticipated that the update proposals from the Strategic Leadership Group will be presented to the next meeting of the Business Transformation Steering Group on 15 January 2018 and will then form part of the final proposals presented to Council on 13 February 2018.

8.2 Transformation Programme

The savings targets associated with the existing Transformation Programme have been updated from those set out in the last report to take cognisance of those proposals which had also been incorporated in the policy savings proposals and which were therefore double counted in error. This includes

proposals included in the Services to Communities review in respect of Welfare Rights (£0.100 million) and Grants (£0.150 million).

The remaining savings target of £0.600 million for the Services to Communities review related to the property rationalisation strand of the review. At a special meeting of the Business Transformation Steering Group on 4 December 2018 the members present were asked to consider officer proposals in respect of this strand and these are now encompassed in a separate report on today's agenda. The savings targets for the Services to Communities review have therefore been amended to reflect the recommendations in that report, with savings targets reflecting the closure of Newbattle Pool and Mayfield Leisure Centre included for 2018/19 onwards.

In addition to the base budget pressures included for Children's Services in section 3 the savings target of £0.274 million previously included for 2018/19 has also been amended to apply from 2019/20 onwards.

Table 6 sets out the revised savings targets for the existing programme which are £1.904 million for 2018/19 rising to £2.239 million by 2021/22. Other than the changes set out above the targets for the other strands are derived from those set out in the Council's Transformation Programme update reports to Business Transformation Steering Group (BTSG).

Table 6: Existing Transformation Programme Savings – 19 December 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Children's Services	0.000	0.335	0.335	0.335
Services to Communities	0.542	0.542	0.542	0.542
Education	0.322	0.322	0.322	0.322
Health & Social Care	1.040	1.040	1.040	1.040
Totals	1.904	2.239	2.239	2.239

The emerging proposals include an updated and expanded Transformation Programme, the current assessment of the savings associated with these strands of work is summarised as follows:-

Table 7: Additions to Transformation Programme – 19 December 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Entrepreneurial Council	0.345	1.785	3.065	4.900
Services with Communities	0.000	0.600	0.700	1.700
Shared Services	0.000	0.085	1.085	2.085
Digital Led Transformation	0.240	0.240	0.240	0.740
Integrated Service Support	0.480	0.980	0.980	0.980
Workforce Planning	0.603	1.085	1.185	1.250
Health & Social Care	0.000	1.040	3.080	4.620
Additions to Programme	1.668	5.815	10.335	16.275

Again it is reiterated to members that the savings targets set out in tables 6 and 7 are predicated on the outcomes of the reviews and any subsequent decisions taken by Council and so remain indicative.

8.3 Asset Management

The budget projections already reflect the full year impact of the first two phases of the Effective Working in Midlothian project. In addition the report to Council on 17 May 2016 in respect of Phase 3, Depots indicated a saving of £0.288 million which for the purposes of the Financial Strategy have been incorporated from 2019/20 onwards.

8.4 Capital and Reserves Strategy

The projected future year's budgets include a provision for the loan charges arising from the borrowing required to support the General Services Capital Plan and also the retention of a cap on borrowing, which had been set at £124 million, and which is currently expected to be exceeded.

An increase in the borrowing cap will inevitably lead to an increase the projected budget shortfalls for later years. In the absence of any other funding support this will in turn require further reductions in the service budgets.

A comprehensive review of the General Service Capital plan is being undertaken with the intention to present an updated plan for consideration by Council on 13 February 2018. This will enable the implications of the Learning Estate Strategy and other emerging investment pressures to be fully considered before presenting a revised Capital Strategy and Plan.

The latest projections for the General Fund Reserve are set out later in this report. A Reserves Strategy, encompassing the other main reserves will be presented alongside the Capital Strategy.

8.5 Operational Savings

The budget projections set out in tables 1 and 2 already reflect the operational savings reported in previous year's budgets. Operational savings cost reductions and financial discipline measures have been identified as part of the emerging Change Programme with the updates projections summarised below.

Table 8: Operational Savings – 19 December 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Investing in Our Workforce	0.000	0.100	0.250	0.300
Financial Discipline	0.100	0.150	0.200	0.250
Cost Reductions	0.080	0.160	0.245	0.250
Workforce Reductions	0.478	1.119	1.149	1.339
Operational Savings	0.658	1.529	1.844	2.139

8.6 Savings

The budget proposals presented to Council on 10 October 2017 include a number of Service Reviews and specific policy cost reductions. Again the latest assessment of savings associated with these is as follows:-

Table 9: Policy Saving Proposals- 19 December 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Service Reviews	1.459	2.703	3.003	3.003
Policy Cost Reductions	4.851	5.708	6.208	6.408
Policy Saving Proposals	6.310	8.411	9.211	9.411

8.7 Fees and Charges

An inflationary increase for fees and charges are estimated to generate an addition £0.080 million in 2018/19 rising to £0.200 million by 2021/22.

8.8 Summary of Financial Strategy

The updated projections incorporating the impact of the various strands of the Financial Strategy set out above and a 3% per annum increases in Council Tax are set out in table 10 below.

Given the remaining budget gap for 2018/19, the overspend position projected for the current financial year and the potential to have to increase the provision for pay awards it is imperative that further cost reduction measures are secured during the current financial year. Accordingly action is being taken across all services to end all unnecessary spend over the remainder of the financial year.

Table 10: Financial Strategy 2018/19 to 2021/22 – 19 December 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Budget Shortfall Table 1	14.081	25.315	35.375	45.478
Less: Change Programme				
Transformation Programme 8.2				
- Existing Programme	(1.904)	(2.239)	(2.239)	(2.239)
- Additions to Programme	(1.668)	(5.815)	(10.335)	(16.275)
Total Transformation Programme	(3.572)	(8.054)	(12.574)	(18.514)
Asset Management 8.3	(0.000)	(0.288)	(0.288)	(0.288)
Operational Savings 8.5	(0.658)	(1.529)	(1.844)	(2.139)
Savings Options 8.6				

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
- Policy Cost Reductions	(4.851)	(5.708)	(6.208)	(6.408)
- Service Reviews	(1.459)	(2.703)	(3.003)	(3.003)
Total Policy Savings	(6.310)	(8.411)	(9.211)	(9.411)
Fees and Charges 8.7	(0.080)	(0.140)	(0.180)	(0.200)
Less:				
Council Tax Increase of 3%	(1.274)	(2.569)	(3.884)	(5.218)
Remaining Budget Gap	2.187	4.324	7.394	9.708

The increase of £1.804 million in the remaining budget gap in 2018/19 since the last report on 10 October 2017 principally attributable to:-

- The increase in the budget shortfall set out in table 3 (£0.586 million);
- The correction of those items which were double counted in the existing Business Transformation Programme (£0.250 million);
- The correction of items which were double counted in the budget shortfall and also in the proposed change programme (£0.572 million);
- Revision of the remaining Services to Communities savings target (£0.058 million); and
- The re-phasing of the Children's Service review savings (£0.274 million).

While the Change Programme summarised above would significantly reduce the projected budget gaps from those previously reported it does not fully address these or give Council any headroom to consider options or indeed allow a contribution to Reserves. It should also be noted that a number of the programme elements continue to be subject to further development and robust review to ensure that officers and members can be confident of deliverability.

Accordingly work is ongoing to develop further proposals, specifically for 2018/19 and also to amend some of the existing proposals to take cognisance of the feedback from the engagement activity. It is anticipated that the update proposals from the Strategic Leadership Group will be presented to the next meeting of the Business Transformation Steering Group on 15 January 2018 and will then form part of the final proposals presented to Council on 13 February 2018.

In addition in cognisance of the budget challenge for 2019/20 and beyond work continues to explore additional savings options as part of the wider service review programme activities, these include:

- The inclusion of a Disability Service Review as part of the next steps for Children's Services Review;
- Efficiencies secured through the Learning Strategy Estate, wider property asset management and asset rationalisation;
- A master plan for the Vogrie Estate and potential income opportunities it creates;

- A further review of the approaches to and resources committed to transportation of people, both clients and staff;
- A broader review of concessions for future consideration.

Given the longer term outlook work will also be required to review and bring forward further proposals in respect of the following areas:-

- Workforce, recognising that employee costs are by far the largest element of the budget;
- The conditions attached to grant settlements, including the implications of maintaining the pupil teacher ratio and of restricting Council Tax increases to 3%.

A final set of proposals in respect of 2018/19 will be presented to Council on 13 February 2018 and in addition the emerging Change Programme for later years will be continually updated to take cognisance of the position for future years grant and pay settlements and demographic changes recognising the critical impact these issues have on the Financial Strategy and the projected budget position.

As the budget for 2018/19 is finalised I will, as Section 95 Officer, require to seek assurance from Directors and Heads of Service that the budget proposals put forward by them for consideration are achievable and the risks associated with delivery have been identified. It is stressed however that ultimately the achievement of savings will be dependent on decisions taken by Council.

9 Governance and Timetable

Each element of the Financial Strategy continues to have governance in place to ensure the timely delivery of the work stream. All budget proposals are being reported through Business Transformation Steering Group and then to Council as appropriate. Responsibility for setting Council Tax, determining budgets and approving savings etc. remains, with full Council.

The full Council has a duty as set out in Section 93 of the Local Government Finance Act 1992 (as amended) to set its Council Tax and a balanced budget for the following financial year commencing 1 April by 11 March and the timetable set out in Table 10 supports the delivery of the Financial Strategy and specifically the determination of the 2018/19 budget and Council Tax levels before the statutory date.

Council should note that all political groups have been given the offer of officer support in terms of both the financial and equalities assessment of any possible alternative budgets proposals they may intend to put forward for 13 February 2018.

Table 11: Timetable – Key Events

Date *	Event	Action
14 December 2017	Grant Settlement	<ul style="list-style-type: none"> • Assessment of grant settlement implications on budget.
19 December 2017	Council	<ul style="list-style-type: none"> • Consideration of update report and initial feedback on engagement.
13 February 2018	Council	<ul style="list-style-type: none"> • Consideration of update report, reflecting grant settlement. • Finalisation of Change Programme and savings proposals. • Recommendations to set Council Tax and determine a budget for 2018/19.

Members should also note that in terms of Section 112 of the Local Government Finance Act 1992 (as amended) it is an offence for members to participate in any vote in respect of setting Council Tax where the member has unpaid Council Tax. Accordingly at the Council meeting on 13 February 2018 members will be required to disclose the fact if this section of the act applies to them and subsequently not vote on any item with respect to the matter.

10 Focussing Resources to Key Priorities

The Financial Strategy is designed to ensure that available resources are as far as possible targeted on delivery of improved outcomes, particularly against the key priorities of:-

- Reducing the gap in learning outcomes
- Reducing the gap in health outcomes
- Reducing the gap in economic circumstances

The Midlothian Community Planning Partnership continues to prioritise the available resources towards the delivery of the partnerships key priorities and the Financial Strategy sets out for partners the parameters the Council is working within and provides a means to better facilitate the sharing of budget and resource planning information.

The Change Programme will be central to ensuring that resources are directed towards the priorities set out in the Midlothian Single Plan.

11 Reserves

The projected position for General Fund Reserves was set out in the Financial Monitoring 2016/17 – General Fund Revenue report to Council on 7 November 2017.

The projected uncommitted General Fund Reserve at 31 March 2018 is £2.102 million. This uncommitted reserve is below the preferred level to provide a contingency in the context of the continuing challenging financial outlook, the uncertainty associated with future years grant settlements, pay awards, the economic impact of Brexit and also the potential costs as a consequence of the Limitation (Childhood Abuse) (Scotland) Act 2017.

As noted earlier as part of the action being taken to address the projected overspend in the current year the Chief Executive has instructed that action be taken across all services to end all unnecessary spend over the remainder of the financial year.

Alongside addressing the projected overspends in the current financial year it would be prudent to secure a budget for 2018/19 which included a contribution to reserves, preferably in the region of £2 million with a resultant available contingent reserve above £4 million.

Table 12 summarises the General Fund Reserve position.

Table 12: Available General Fund Reserve 31 March 2018 – 19 December 2017

	£million
General Fund Balance at 31 March 2018	6.846
<i>Earmarked for specific purposes</i>	
• Earmarked for Council Transformation	(3.737)
• Devolved School Management	(1.007)
Available Contingent Reserve at 31 March 2018	2.102

In addition the unallocated balance on the Capital Fund at 31 March 2018 is projected to be £12.514 million.

12 Report Implications

12.1 Resources

Whilst this report deals with financial issues there are no financial implications arising directly from it.

12.2 Risk

Within any financial projections, there are a number of inherent assumptions in arriving at figures and budget provisions and therefore risks that may be faced if costs change or new pressures emerge.

The following key risks and issues are highlighted in the context of this report:

- The economic outlook and decision by Scottish Government on future years grant settlements and grant distribution;

- Given the nature of the savings options incorporated in the budget proposals the increase risk of non-delivery or late delivery of planned savings, including those arising from reductions in the staffing establishment;
- The risk to service provision and service users associated with a continued decline in available resources to fund services;
- Outstanding pay award settlements and the implications of the National Living Wage for external service providers;
- Actual school rolls exceeding those provided for in the budget;
- The impact of the wider economic climate on range of factors including: inflation, interest rates, employment, tax and income levels and service demands;
- Cost pressures, particularly demographic demand, exceeding budget estimates;
- The impact of Universal Credit, and potential pension changes;
- The impact of the Scottish Governments response to the Barclay Review of non-domestic rates on both the cost of existing services and the emerging budget proposals;
- The costs of implementation of national policies varying from the resources provided by Government; and
- Unplanned capital investment requirements and associated cost.

The Financial Strategy aims to mitigate a number of these risks by setting out the key assumptions on which forward plans are based, and through the Change Programme activities, setting out the early identification of future saving proposals.

The projections set out in this report highlight the severity of the challenge ahead for the term of this Council and the extent to which service provision will have to be significantly transformed and or reduced.

The work of the Strategic Leadership Group, led by the Chief Executive, to develop and bring forward a comprehensive set of budget options for Council's consideration is critical to enable Council to address the projected budget gaps and in securing financial sustainability for the continued delivery of services. Work continues as part of the assurance process to review the proposals, the value of savings attached these and to develop implementation plans.

The severity of the challenge is such that Council will require to approve a range of proposals on 13 February 2018 which not only achieves a balanced budget for 2018/19 but which will also contribute to reducing future year's budget shortfalls. The risk of not doing so would be the potential elimination of available reserves and so severely limiting the Council's ability to deal with unforeseen or unplanned events.

12.3 Single Midlothian Plan and Business Transformation

Themes addressed in this report:

- Community safety
- Adult health, care and housing
- Getting it right for every Midlothian child
- Improving opportunities in Midlothian
- Sustainable growth
- Business transformation and Best Value
- None of the above

12.4 Impact on Performance and Outcomes

The Financial Strategy facilitates decision on how Council allocates and uses its available resources and as such has fundamental implications for service performance and outcomes. The budget projections indicate that in 2021/22 the Council will have available in the region of £180 million for the provision of services and the pursuit of key outcomes as set out in the Single Midlothian Plan.

12.5 Adopting a Preventative Approach

Whilst the proposals in this report do not directly impact on the adoption of a preventative approach, an effective Financial Strategy in turn allows resources to be prioritised to support prevention.

12.6 Involving Communities and Other Stakeholders

On 10 October 2017 Council agreed to proceed to engage with the community on the budget and change programme through Shaping our Future, the consultation strand of the Delivering Excellence framework. The engagement runs to 14 December 2017 has a focus on informing the community and other stakeholders of the financial and service challenges and provides a means to engage on the change programme.

Interim feedback from the engagement activity is set out in appendix 1 and as set out earlier, a detailed report will be prepared and made available to all members early in the new year and also considered by the Business Transformation Steering Group on 15 January 2018;

In addition, there continues to be engagement with the recognised Trade Unions on the Council's financial position and service challenges. Officers have met regularly with Trade Union colleagues to consult with them on the overall change programme with separate meetings held within each Directorate where necessary to allow a more detailed discussion of the proposals. It is expected that the Trade Unions will also seek an update at the Joint Consultative Group meeting on 12 December 2017.

12.7 Ensuring Equalities

The Financial Strategy and the proposals which support financial sustainability has been developed within the context of the Midlothian Single Plan, ensuring that resources are directed towards the key priorities of reducing the gap in learning, health and economic circumstance outcomes.

The Financial Strategy and the proposals in the Change Programme also reflect Midlothian Council's commitment to the ethos of the Equality Act 2010

with careful consideration of the interests of the most vulnerable in our communities through the equality impact assessment (EqIA) of all the proposals.

Copies of individual assessments were published on 10 October 2017 and an updated overarching EqIA is also set out in appendix 2. What the EqIAs continue to demonstrate is the Council's undertaking to clearly identify when the most vulnerable may be affected by budget proposals, and to work to develop where possible mitigating actions to reduce any further negative impacts. Where necessary this work will be undertaken in the coming months.

In addition, these actions underline the Council's commitment in its Midlothian Equality Plan 2017 – 2021 to tackle inequality and promote inclusion. These actions also will allow the Council to plan and deliver services which meet the needs of our diverse communities and respond to the changes ahead.

12.8 Supporting Sustainable Development

There are no direct sustainability issues arising from this report.

12.9 Digital Issues

There are no direct digital implications arising from this report.

13 Summary

This report provides:-

- An assessment of future years Scottish Government Grant;
- Updated budget projections for 2018/19 to 2021/22;
- A sensitivity analysis reflecting the potential impact of different pay and grant settlement scenarios years;
- Details of the arrangements for the delegation of resources to the Midlothian Integration Joint Board;
- An update on the Change Programme aimed at addressing the projected budget shortfalls;
- Initial feedback from the budget engagement activity;
- An update on Reserves.

14 Recommendations

Council is recommended to:-

- a) Note the position in respect of the Scottish Government Grant Settlement as set out in section 2 and received a verbal update on the initial analysis of the grant settlement announced on 14 December 2017;
- b) Note the current projected cost of services, key assumptions and resultant budget shortfalls as set out in section 3 and endorse the key assumptions on which the budget projections are based;
- c) Note the continuing uncertainties and the potential impact as outlined in the differing scenarios as set out in section 6;

- d) Instruct the Head of Finance and Integrated Service Support to advise the Midlothian Integrated Joint Board of the indicative allocation of £38.086 million for 2018/19 and the projected allocations for later years as set out in section 7;
- e) Note the updated assessment of the proposed Change Programme and projected future years Council Tax increases and the impact on the Financial Strategy as set out in table 10;
- f) Note that incorporating the emerging Change Programme the indications are that there would still be a budget gap of £2.187 million for 2018/19 rising to £9.708 million by 2021/21, though these are heavily dependent on the assumptions detailed in the report;
- g) Note that further proposals, specifically for 2018/19 along with amendments existing proposals to take cognisance of the feedback from the engagement activity will be presented to the next meeting of the Business Transformation Steering Group on 15 January 2018 and will then form part of the final proposals presented to Council;
- h) Note the initial feedback on the budget engagement and agree a detailed report be prepared and made available to all members early in the New Year and that it is also considered by the Business Transformation Steering Group on 15 January 2018;
- i) Note that there continues to be engagement with the recognised Trade Unions on the Council's financial position and service challenges;
- j) Note the governance arrangements and timetable set out in section 9;
- k) Note the severity of the financial challenge and also the risks as set out in section 12.2.
- l) Note that a further report will be presented to Council on 13 February 2018 to allow Council to determine Council Tax and set a balanced budget for 2018/19.

Date 11 December 2017

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Appendix 1 – Interim Shaping Our Future engagement report

Appendix 2 – Updated EQiA