

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 update on 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;
- An update on the arrangements for the delegation of resources to the Midlothian Integration Joint Board;
- An overview of the Change Programme aimed at addressing the projected budget shortfalls;
- 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 27 June 2017 and provided an updated assessment of projected budgets shortfalls through to 2021/22. At that meeting Council approved a budget timetable which provided for Change Programme proposals to be presented to this meeting of Council to facilitate a period of engagement as part of the process to determine the 2018/19 budget early in 2018.

A draft proposals document setting out details of the Change Programme was presented to the Business Transformation Group on 28 August 2017. The proposals were subsequently subject to further scrutiny and refinement by the Strategic Leadership Group and at the time of writing this report that work is ongoing. Accordingly this report includes a summary of the proposals in section 8, Change Programme, and recommends special meetings of Business Transformation Steering Group on 2 October 2017 and Midlothian Council on 10 October 2017 be arranged to allow full consideration of the detailed Change Programme proposals.

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.

On 5 September 2017 The First Minister set out her Government's "Programme for Government" for the year ahead. This includes "...removing the 1% pay cap from 2018-19. Future pay policy will take account of the cost of living, continue to protect the lowest paid and ensure public sector budgets remain in balance". Given the specific reference made to Teachers it is understood that Government intend that removing the pay cap would extend to local government employees. The consumer price index is currently 2.9%, significantly higher than the 1% included in earlier financial projections. At this point it is unclear what, if any, additional resources Government may provide to Local Authorities to support increases in the pay bill which take account of the cost of living.

The increase in the pay bill as a result of the 2017 Local Government Workers settlement (the higher of 1% or £350) was approximately 1.4%, which had to be accommodated within the overall grant settlement. As such it is considered that if there is additional support from Government injected into the settlement to support pay increases that it is most probable that this would be unlikely to cover the first 1.5% of any award. Accordingly the provision for pay awards set out in section 5 has been increased from 1% to 1.5% per annum, with the assumption that the cost of awards above this would be matched by funding through the grant settlement. This revision adds an additional £0.600 million to the 2018/19 budget shortfall, rising to £2.500 million by 2021/22.

The position will be reviewed once the Government's budget is published and an assessment is made of the extent to which Government may provide support through the grant settlement for higher pay awards. 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.

The full implications of the "Programme for Government" for the public sector, and specifically Local Government, will become clearer over the coming months and in particular with the publication of the Government's draft budget for 2018/19. The expectation is that the Cabinet Secretary for Finance and the Constitution will publish the Scottish Government budget proposals for 2018/19 in December 2017. This will follow on from the publication of the UK Government's first Autumn Budget. It is still anticipated that Scottish Government will publish a budget only for the year ahead and will not return to the publication of three year budgets. 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.

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.

There are three main factors which will influence the level of grant support Council might expect for 2018/19 and beyond. 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. The other main factors will be 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 etc. the impact of Scottish Government's tax and spending priorities will only become fully apparent when the budget is published in December 2017.

The CIPFA Directors of Finance section have engaged an economist to interpret the available data and his assessments continue to indicate a continued 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 are 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 is based on reductions in grant at a similar level to the original proposed 2017/18 settlement. This is an average 3.25% per annum cash reduction at a national level, 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 by up to 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 are continually updated to reflect the latest information available and work will continue to refine the budget projects though the remainder of 2017. Changes will be incorporated into an update report proposed for Council in December 2017.

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 will also result in 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;
- 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 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 – 26 September 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Cost of Services	205.101	213.520	220.986	228.565
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	13.495	24.629	34.689	44.792

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 are very much 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 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 for future years. Critically they highlight the severity of the challenge ahead for the term of 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 – 26 September 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Opening Shortfall	3.970	13.495	24.629	34.689
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	0.547	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	0.324	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	(1.296)	(0.358)	(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	13.495	24.629	34.689	44.792

The principal movement from the figures set out in the 27 June 2017 report are as follows.

Table 3: Movement from 27 June 2017 to 26 September 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Shortfall 27 June 2017	12.933	23.770	33.458	43.184
Pay Awards	0.600	1.200	1.850	2.500
Reinstatement of Community Policing Teams	0.563	0.569	0.575	0.581
Supported Bus Services	0.009	0.009	0.009	0.009
Revisions to Grant Projections	(0.294)	(0.569)	(0.825)	(1.064)
Revision to Planning Income	(0.036)	(0.070)	(0.098)	(0.138)
Other Base Budget Movements	(0.280)	(0.280)	(0.280)	(0.280)
Shortfall 26 September 2017	13.495	24.629	34.689	44.792

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 – 26 September 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Scenario 1				
Central Assumption	13.495	24.629	34.689	44.792
Cash Flat Government Grant	(3.172)	(6.487)	(9.731)	(12.905)
Amended Shortfall	10.323	18.142	24.958	31.887
Scenario 2				
Central Assumption	13.495	24.629	34.689	44.792
Revised Pay Award Assumption	1.800	3.600	5.550	7.500
Amended Shortfall	15.295	28.229	40.239	52.292

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 (MIJB). For 2017/18 the allocation was set at £37.510 million. Whilst the projected budget shortfalls set out earlier incorporate inflationary uplifts and a sum for demographic cost pressures in respect of services delegated to the IJB the draft change programme also provides these to be significantly offset.

Discussions are continuing with officers of the MIJB 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 MIJB's Financial Strategies.

This approach will support the MIJB 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 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.

Taking cognisance of the extent of savings anticipated to secure a balanced budget for 2018/19 and the continued challenge for later years the Chief Executive has tasked Directors and Heads of Service to bring forward options aimed at addressing the projected budget gaps.

A draft proposals document setting out details of the change programme was presented to the Business Transformation Steering Group on 28 August 2017. The proposals were subsequently subject to further scrutiny and refinement by the Strategic Leadership Group and at the time of writing this report that

work is ongoing. Accordingly this report includes a summary of the proposals and recommends special meetings of Business Transformation Steering Group on 2 October 2017 and Midlothian Council on 10 October 2017 be arranged to allow full consideration of the detailed budget proposals.

8.2 Transformation Programme

The savings targets associated with the existing Transformation Programme are set out in table 5 and total £2.550 million for 208/19 rising to £2.646 million by 2021/22. These are derived from those set out in the Council's Transformation Programme update reports to Business Transformation Steering Group (BTSG).

Table 5: Existing Transformation Programme Savings – 26 September 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Children's Services	0.274	0.335	0.335	0.335
Services to Communities	0.850	0.850	0.850	0.850
Education	0.426	0.461	0.461	0.461
Health & Social Care	1.000	1.000	1.000	1.000
Totals	2.550	2.646	2.646	2.646

The emerging proposals include an updated and expanded transformation programme summarised as follows:-

Table 6: Proposed additions to Transformation Programme - 26 September 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Entrepreneurial Council	0.415	1.905	3.235	5.125
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	0.730	1.230	1.230	1.230
Workforce Planning	0.595	1.207	1.307	1.372
Health & Social Care	0.000	1.040	3.080	4.620
Additions to Programme	1.980	6.307	10.877	16.872

The savings targets set out in tables 5 and 6 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 set out in this report. 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 now present an updated plan for consideration by Council in November 2017. This will enable the implications of the Learning Estate Strategy 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. Further operational savings cost reductions and financial discipline measures have been identified as part of the emerging Change Programme are summarised below.

Table 7: Operational Savings - 26 September 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 emerging budget proposals include a number of Service Reviews and specific policy cost reductions summarised as follows, full details will be presented to the proposed special meetings of BTSG on 2 October 2017 and Midlothian Council on 10 October 2017.

Table 8: Policy Saving Proposals- 26 September 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Service Reviews	1.652	2.896	3.196	3.196
Policy Cost Reductions	4.758	5.481	5.851	5.921
Policy Saving Proposals	6.410	8.377	9.047	9.117

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 9 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.

Table 9: Financial Strategy 2018/19 to 2021/22 – 26 September 2017

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Budget Shortfall Table 1	13.495	24.629	34.689	44.792
Less: Change Programme				
Transformation Programme 8.2				
- Existing Programme	(2.550)	(2.646)	(2.646)	(2.646)
- Additions to Programme	(1.980)	(6.307)	(10.877)	(16.872)
Total Transformation Programme	(4.530)	(8.953)	(13.523)	(19.518)
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				
- Policy Cost Reductions	(4.758)	(5.481)	(5.851)	(5.921)
- Service Reviews	(1.652)	(2.896)	(3.196)	(3.196)
Total Policy Savings	(6.410)	(8.377)	(9.047)	(9.117)
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	0.543	2.773	5.923	8.312

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.

In addition there are a number of additional savings options currently being developed 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.

To secure additional savings to, as a minimum, address the remaining budget gap for 2018/19, and in cognisance of the projected overspend position for the current financial year it is proposed to operate a Voluntary Severance Early Retirement scheme in the autumn of 2017 in accordance with the existing VSER Policy framework. This is expected to secure immediate additional savings.

For later years further work is also 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%.

The emerging Change Programme will be continually updated to take cognisance of the position for future years grant settlements and demographic changes, recognising the critical impact both of these issues have on the Financial Strategy and the projected budget position.

As the Financial Strategy develops over the coming months 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. 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 clear 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 Midlothian 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.

Table 10: Timetable – Key Events

Date *	Event	Action
26 September 2017	Council	<ul style="list-style-type: none"> • Consideration of updated projections. • Update on Financial and Strategy and Capital Plans. • Summary of Change Programme and updated budget gap.
10 October 2017	Special Council	<ul style="list-style-type: none"> • Consideration of Change Programme and savings proposals and approval to proceed to engagement.
October/November 2017	Engagement	<ul style="list-style-type: none"> • Shaping our Future engagement on Financial Strategy and Change Programme.
Mid 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 feedback on engagement.
Late January or Early 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.

** Based on current meeting schedule and so may require revision. Interim reports will be presented to Council as necessary.*

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 proposed for late January/Early February 2018 members would be required to disclose the fact if this section of the act applies to them and subsequently not vote on any question 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 29 August 2017.

The projected uncommitted General Fund Reserve at 31 March 2018 is £2.252 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 to come from the historic child abuse enquiry. Accordingly 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 11 summarises the General Fund Reserve position.

Table 11: Available General Fund Reserve 31 March 2018 – 27 September 2017

	£million
General Fund Balance at 31 March 2018	6.070
<i>Earmarked for specific purposes</i>	
• Earmarked for Council Transformation	(3.818)
Available Contingent Reserve at 31 March 2017	2.252

In addition the unallocated balance on the Capital Fund at 31 March 2018 is projected to be £18.397 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 will be critical to enable Council to address the projected budget gaps and securing financial sustainability for the continued delivery of services. Whilst the emerging impact of the Change Programme is set out in this report, work will continue over the autumn as part of the assurance process to review the proposals and the value of savings attached these.

The severity of the challenge is such that Council will require to approve a range of proposals over the coming months which not only achieves a balanced budget for 2018/19 but which will also contribute to reducing future years budget shortfalls. The risk of not doing so would be the potential elimination of 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

The proposed timetable set out in section 9 includes the continuation of Shaping our Future, the engagement strand of the Delivering Excellence framework. This has a focus on informing the community and other stakeholders of the financial and service challenges and provides a means to engage on the emerging change programme.

In addition, there continues to be engagement with the recognised Trade Unions on the Council's financial position and service challenges.

12.7 Ensuring Equalities

The Financial Strategy and the proposals which support financial sustainability will be developed within the context of the Midlothian Single Plan, ensuring that resources are directed towards key priorities. They will also reflect Midlothian's commitment to the ethos of the Equality Act 2010 with consideration of the interests of the most vulnerable in our communities through equality impact assessment for all the proposals.

A draft overarching EQIA encompassing the budget proposals is being prepared alongside the finalisation of the Change Programme and will be included as an appendix to the report to the proposed special meeting of Midlothian Council. This draft EQIA report will also be updated as the revenue budget for 2018/19 is finalised with the final report incorporated in the report considered by Council when it sets the 2018/19 budget and Council Tax early in 2018.

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 update on future years Scottish Government Grant;
- Budget projections for 2018/19 to 2021/22;
- A sensitivity analysis reflecting the potential impact of different pay and grant settlement scenarios years;
- An update on the arrangements for the delegation of resources to the Midlothian Integration Joint Board;
- An overview of the Change Programme aimed at addressing the projected budget shortfalls;
- 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;
- 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) Note the ongoing work to support the development the Midlothian Integrated Joint Board's own Financial Plans;
- e) Note that there continues to be engagement with the recognised Trade Unions on the Council's financial position and service challenges;
- f) Note the impact of the proposed Change Programme and projected future years Council Tax increases and the impact on the Financial Strategy as set out in table 9;
- g) Agree to call a special meeting of the Business Transformation Steering Group on 2 October 2017 and a special meeting of Midlothian Council on 10 October 2017 to consider the detailed Change Programme and remit to the Director Resources to finalise arrangements for these;
- h) Note the governance arrangements and timetable set out in section 9, which incorporate the special meeting of Midlothian Council;
- i) Note that after incorporating the emerging Change Programme the indications are that there would still be a budget gap of £0.543 million for 2018/19 rising to £8.312 million by 2021/21, though these are heavily dependent on the assumptions detailed in the report;
- j) Agree to operate a Voluntary Severance Early Retirement scheme in the autumn of 2017 in accordance with the existing VSER Policy framework and delegate the detailed arrangements for this to The Chief Executive in consultation with The Leader of The Council.
- k) Note the severity of the financial challenge and also the risks as set out in section 12.2.
- l) Otherwise note the contents of the report.

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