



## **Financial Strategy 2015/16 to 2017/18**

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

#### **1 Purpose of Report**

This report provides Council with a further update on the delivery of the Financial Strategy approved by Council on 4 February 2014.

It includes an update on:-

- Scottish Government Grant Settlements;
- Projections for 2015/16 and 2016/17;
- Initial projections for 2017/18;
- Delivery of the strands of the Financial Strategy, including the Transformation Programme; and
- Reserves.

#### **2 Background**

The core objective of the Financial Strategy is to facilitate the Council's continued financial sustainability during a continuing period of unprecedented constraint. Whilst the Financial Strategy now encompasses the period to 2017/18 the prospects for later years remain challenging with an extended period of financial constraint expected to continue well into the next decade. As a consequence, Midlothian in common with all Councils will need to reposition itself through the withdrawal and dilution of services and by having a greater emphasis on those in the community who are the most disadvantaged and vulnerable.

The need to transform and reposition services has never been greater and the work streams which form the Financial Strategy provide a means to secure financial sustainability, incorporating the actions the Council will take to address predicted budget shortfalls and at the same time prioritise available resources to focus these on the delivery of the Council's priority outcomes of Early Years, Positive Destinations and Economic Growth and its priority localities.

#### **3 Scottish Government Grant Settlement**

The projections included in the Financial Strategy have been updated to reflect a comprehensive review of the current grant settlement and in particular the impact of additional resources for new burdens and redeterminations. In addition the Financial Strategy continues to assume a 1% reduction in grant in both 2016/17 and 2017/18.

#### 4 Council Tax

The Financial Strategy is based on a continuing Council Tax freeze with Band D Council Tax remaining at £1,210. The Council Tax income detailed in table 1 has been updated to reflect the latest Council Tax Base and also reflects the additional income from the projected increase in the number of properties.

#### 5 Cost of Services

Table 1 provides an update on the projected costs of providing services and continues to be based on a number of assumptions on cost and income over the period. Work will continue to review and update these projections through the remainder of the year. As such it is inevitable that these projections will change over the coming months.

The key assumptions reflected in the budget projections include:

##### **Inflationary and Other Cost Pressures on existing Service Costs:-**

- An increase in the assumptions made for pay awards with 1.5% provided in each of the years (previously 1%) and contractual inflation on other costs for each of the years;
- A provision for increased national insurance costs as a result of the Public Services Pensions Act 2013. Current estimates are an increased cost for the Council from 2016/17 of £2 million per annum, with no compensating increase in government funding;
- Borrowing costs reflect the General Services Capital Plan; and
- The introduction of food waste collection from 2015.

##### **Demographic Cost Pressures**

- A provision for additional social care services demographic cost pressures of £1.1 million per annum.
- A provision for increasing school rolls of £0.405 million in 2015/16, a further £0.407 million in 2016/17 and £0.400 million in 2017/18.

There are further signs of increasing inflationary cost pressures which may impact on the budget projections, particularly in relation to pay and the provision of social care services.

The projected budget shortfall reflecting the above is detailed in table 1.

**Table 1: Projected Budget Shortfalls 2015/16 to 2017/18 – 23 September 2014**

	2015/16 £m	2016/17 £m	2017/18 £m
Cost of Services	196.783	203.711	208.236
Less: Council Tax	40.000	40.500	41.000
Less: Scottish Government Grant	154.097	152.241	150.441
	<b>2.686</b>	<b>10.970</b>	<b>16.795</b>

In broad terms the shortfall arises for the following reasons:

**Table 2: Analysis of Shortfalls – 23 September 2014**

	2015/16 £m	2016/17 £m	2017/18 £m
Opening Shortfall	-	2.686	10.970
Pay Inflation	1.645	1.771	1.797
Contractual and other inflation	1.027	1.062	1.062
Pensions Act	-	2.000	-
Food Waste Collection	0.264	0.283	-
Demographics: Care	1.100	1.100	1.100
Demographics: School Rolls	0.405	0.407	0.400
Scottish Government Grant	(0.910)	1.856	1.800
Council Tax: Additional Income	(1.184)	(0.500)	(0.500)
Other Movements	0.339	0.305	0.166
<b>Totals</b>	<b>2.686</b>	<b>10.970</b>	<b>16.795</b>

The principal changes since the last report to Council on 24 June 2014 are attributable to the following:-

**Table 3: Analysis of Shortfall – 4 February 2014 to 24 June 2014**

	2015/16 £m	2016/17 £m	2017/18 £m
24 June 2014	3.320	11.357	-
Pay Inflation	0.481	1.078	-
Scottish Government Grant	(0.910)	0.356	-
Council Tax	(0.700)	(0.600)	-
Other /Initial Projection	0.495	(1.221)	16.795
<b>23 September 2014</b>	<b>2.686</b>	<b>10.970</b>	<b>16.795</b>

The projected shortfall of £16.795 million equates to approximately 8% of net revenue expenditure. As previously indicated 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, approximately £20 million;
- Specific conditions, for example the maintenance of teacher numbers, £42.4 million; and
- Growing demand for services through demographic pressures, Care Services £52 million.

These elements account for £114 million or 60% of current expenditure. The £16.795 million shortfall therefore principally falls on the remaining budgets and equates to an 18% reduction.

## **6 Financial Strategy**

### **6.1 Overview**

The approved Financial Strategy provides for the Council to take forward actions which fall into three categories:

- **Efficiencies:** Actions which aim to reduce costs of Council services without changing service levels as far as the public are concerned;
- **Investment:** Actions which aim to reduce the need for Council services or reduce the cost of services in future;
- **Retrenchment:** Actions which reduce the Council's role in terms of the services it provides and for whom it provides them.

These support 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.

### **6.2 Transformation Programme**

The Transformation Programme is central to the delivery of the Financial Strategy, delivering both efficiencies and transformational change in service provision. In addition to ongoing work on Procurement and Integrated Service Support the current Transformation Programme includes:

- Energy;
- Customer Service;
- Income Maximisation;
- Education;
- Services to Communities;
- Externalisation/In-sourcing;
- Children's Services;
- Integrated Health and Social Care;
- School Catchments.

Although there are no savings targets attached to the Integration of Health and Social Care or School Catchments their inclusion in the Transformation Programme reflects the importance of these to future year's financial sustainability.

The latest assessment of the savings targets is set out in table 4 and represents a reduction of £0.175 million in 2015/16 and 2016/17 from the targets set out on 23 June 2014. This reflects an adjustment to the delivery timescale of the saving target for Customer Services Review which now impacts in 2016/17 onwards.

The assessment of the revised targets is derived from the work which has been carried out in the period since 24 June 2014. Work continues to substantiate the targets for Income Maximisation and Externalisation/In-sourcing and as such these targets for these remain indicative. Otherwise the savings targets have a greater degree of confidence of delivery, recognising however that ultimately the achievement of the savings will be dependent on decisions taken by Council.

**Table 4: Council Transformation Programme – 23 September 2014**

	<b>2015/16</b>	<b>2016/17</b>	<b>2017/18</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
Integrated Service Support	0.750	1.500	1.500
Energy	0.000	0.217	0.217
Customer Service	0.000	0.175	0.350
Income Maximisation	0.075	0.150	0.150
Education	0.150	0.300	0.300
Services to Communities	0.300	0.750	1.350
Externalisation/In-sourcing	0.000	0.500	1.000
Children's Services	0.350	0.700	0.700
<b>Totals</b>	<b>1.625</b>	<b>4.292</b>	<b>5.567</b>

Further details are set out in the Council Transformation Programme update report to Business Transformation Steering Group on 25 August 2014.

### **6.3 Workforce Strategy**

There are three main elements of the Workforce Strategy strand

- Management Review;
- VSER;
- Workforce Planning.

#### **Management Review**

The Management Review approved by Council on 13 May 2014 is now projected to achieve savings of £0.990 in 2015/16 rising to £1.179 million in 2017/18, £0.770 million of which represents savings which are already reflected in the Integrated Service Support review targets detailed in section 6.2 with the balance of £0.220 million in 2015/16 rising to £0.409 in 2017/18 further reduces the budget shortfall.

## VSER

The financial implications of VSER are reported elsewhere on today's agenda.

**Table 5 – VSER analysis 23 September 2014**

	2015/16 £m	2016/17 £m	2017/18 £m
VSER Savings already reflected in Financial Strategy:			
• ISS Review	0.232	0.268	0.266
• Management Review	0.633	0.678	0.673
• Other	0.135	0.132	0.131
<b>Sub Total</b>	<b>1.000</b>	<b>1.078</b>	<b>1.070</b>
Additional VSER Savings:			
• Teachers	0.653	0.558	0.467
• Other	0.373	0.375	0.377
<b>Sub Total</b>	<b>1.026</b>	<b>0.933</b>	<b>0.844</b>
<b>General Fund Total</b>	<b>2.026</b>	<b>2.011</b>	<b>1.914</b>
HRA Total	0.035	0.035	0.035
<b>Overall Total</b>	<b>2.061</b>	<b>2.046</b>	<b>1.949</b>

## Workforce Planning

An effective workforce strategy supports the delivery of services by linking workforce planning and development requirements to the Council's strategic and service priorities. Following on from the management review and taking cognisance of the VSER scheme each service is now preparing workforce plans and reviewing staffing establishments.

As the elements of the workforce strategy are developed and savings quantified they will be fully reflected in the Financial Strategy.

## 6.4 Local Government Staff Pay, Grading and Terms and Conditions

On 25 March 2014 Council considered a report on the Review of Local Government Staff Terms and Conditions by the Director, Resources.

Council agreed to:-

- a) Note the arrangements being established to review Pay, Grading, Terms and Conditions of local government staff;
- b) To note the intention to provide an update at June 2014 Council meeting;
- c) Agree the scope and objectives as set out in section 2.3; and
- d) Review further reports in due course.

In this regard the Director, Resources has established the review with research and analysis of both the existing Council terms and conditions and those of comparator organisations being progressed with a view to commencing detailed negotiations with the relevant Trades Unions in August 2014. Negotiations on the issue of Holiday Pay, which is reported elsewhere on today's agenda, has taken priority over recent weeks and as such has impacted on the review of Terms and Conditions. As the position with Holiday Pay progresses the longer term implications for the review of Terms and Conditions will be assessed and a further update will be provided to Council in due course.

## **6.5 Asset Management**

Phase 2 of the EWiM project is underway and is reflected in the Financial Strategy. A Seminar of Council on EWiM has also been arranged for 7 October 2014.

Council approved a review of the existing Public Private Partnership contracts and instructed the Director, Resources to progress this. The Director, Resources has subsequently agreed the scope for an in depth review with The Scottish Futures Trust who have been engaged to undertake the in depth review with findings expected to be reported later in the year.

## **6.6 Borrowing Costs**

The projected budget shortfall set out earlier in table 1 reflects the General Services Capital Plan Strategy approved by Council.

## **6.7 Service Reviews**

The position remains as reported on 24 June 2014.

## **6.8 Efficiency and Financial Discipline**

The first phase of this strand encompassed a review of existing budgets provisions to assess which existing budget provisions could be reduced or simply removed in the current and future years as a consequence of the underspend achieved in 2013/14. At this point it is expected that Financial Discipline savings totalling £0.750 million can be achieved without any detrimental impact on service provision.

In light of the savings secured as a result of the 2014/15 position and the inflationary pressures on budgets it is considered prudent to reduce the efficiency targets for 2015/16 onwards to 0.5% or £0.450 million per annum. These efficiency savings targets recognise the need for all Services to continue to exercise strong financial discipline, improved productivity and demonstrate efficiency ensuring that costs are controlled, unnecessary expenditure ceases and that there is clearly defined accountability for expenditure commitments.

Work continues to be progressed through Strategic Leadership Group to secure further operational efficiencies.

## 6.9 Summary of Financial Strategy

The latest projections of impact of the various strands of the Financial Strategy are as follows. As the strands are further developed the Financial Strategy will be updated to fully reflect the emerging proposals.

**Table 6: Financial Strategy 2015/16 to 2017/18**

	<b>2015/16</b>	<b>2016/17</b>	<b>2017/18</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
Budget Shortfall	2.686	10.970	16.795
<b>Less Strands:</b>			
Transformation Programme (6.2)	1.625	4.292	5.567
Workforce Strategy (6.3)			
• Management Review	0.220	0.409	0.409
• VSER	1.026	0.933	0.844
Terms & Conditions (6.4)	-	-	-
Asset Management (6.5)	0.139	0.277	0.277
Service Reviews (6.7)	0.260	0.560	0.560
Efficiency/Financial Discipline(6.8)	0.750	1.200	1.650
<b>Projected Budget Shortfall / (Surplus)</b>	<b>(1.334)</b>	<b>3.299</b>	<b>7.488</b>

Whilst the figures in table 6 present a broadly similar position for 2015/16 and 2016/17 from that reported on 24 June 2014 they remain projections and as such will inevitably change as assumptions are reviewed the budget is further refined.

Whilst the work undertaken since the last report provides a greater degree of confidence of delivery of the transformational savings it is important to note that ultimately the achievement of these savings will be dependent on decisions taken by Council.

As set out earlier in the report there are already signs of increasing inflationary cost pressures which may adversely impact on the budget projections, particularly in relation to pay and the provision of social care services. Maintaining financial stability through the extended period of financial austerity will therefore remain a significant challenge for the Council.

## 6.10 Service Reductions

Ultimately if the actions set out in sections 6.2 to 6.8 do not bridge the budget shortfall then Council will need to consider policy changes, including the withdrawal from, or dilution of services.



## 7 Governance and Timeline

The timetable outlined in table 7 below provides for regular reports to ensure that Council is kept abreast of developments and provided with the most up-to-date projections. In addition each element of the Financial Strategy will have clear governance in place to ensure the timely delivery of the workstream, with proposals being reported through Business Transformation Steering Group and then to Council as appropriate.

The timetable below sets out the proposed schedule for Financial Strategy update reports to Council, together with details of the proposed schedule for other financial reports over the remainder of the budget period, to allow 2015/16 budget decisions and Council Tax levels to be determined in advance of the statutory deadline of 11 March 2015.

**Table 7: Budget Report Timetable**

<b>Council Meeting</b>	<b>Reports</b>
4 November 2014	Financial Strategy Update Q2 Financial Monitoring
16 December 2014	HRA budget Capital plan Financial Strategy Update incorporating: <ul style="list-style-type: none"> <li>• Final projections</li> <li>• Council Tax</li> <li>• Agreement of budget for 2015/16.</li> <li>• Indicative budget for 2016/17.</li> </ul>
10 February 2015	Further Financial Strategy report if required.

The 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.

Whilst the expectation is that Band D Council Tax will remain at £1,210 per annum, Council are reminded that in terms of Section 112 of the Local Government Finance Act 1992 (as amended) it is an offence to participate in any vote in respect of setting Council Tax where the member has unpaid Council Tax. Members are required to disclose the fact this section of the act applies to them and not vote on any question with respect to the matter.

## 8 Focussing Resources to Key Priorities

As previously reported the Financial Strategy will help ensure that available resources are as far as possible targeted on delivery improved outcomes, particularly against the key priorities of Early Years, Positive Destinations and Economic Growth. The Midlothian Community Planning Partnership is working collectively 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. As the work of the

Midlothian Community Planning Partnership progresses it will be reflected in the Financial Strategy.

## 9 Reserves

The latest projection of useable reserves at 31 March 2015 is as follows:-

**Table 8 –Useable Reserves – 31 March 2015**

	<b>Total £m</b>	<b>Uncommitted £m</b>
General Fund Reserve	11.413	11.199
HRA Balance	21.073	8.039
Capital Fund	8.558	2.558
Repairs and Renewal Reserve	2.553	0.000
<b>Total Useable Reserves</b>	<b>43.597</b>	<b>21.796</b>

It is necessary for the Council to retain reserves to meet unplanned or unforeseen costs. In terms of the General Fund Council agreed on 4 February 2014 that a prudent minimum level of general reserve be £8.000 million or 4% of net expenditure. Whilst the uncommitted element of the General Fund Reserve exceeds £8.000 million, it is anticipated that the extent of change will require continued one off investment or one off costs over the period.

The uncommitted balance on Capital Fund reflects the decisions of Council on 4 February 2014 and is retained to provide for unforeseen capital expenditure and to provide flexibility between financial years, its utilisation is subject to annual review.

Repairs and Renewal Reserves are fully committed. An update on the position with the HRA Balance is encompassed in a separate report on today's agenda.

## 10 Report Implications

### 10.1 Resources

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

### 10.2 Risk

Within any financial plan 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:

- Impact of economic climate on range of factors including: inflation, interest rates, employment, tax and income levels, service demands;
- Outstanding pay award settlements;

- Decision by Scottish Government on future years grant settlements and grant distribution;
- Extreme weather events (or other unforeseen events) and provision for immediate response as well as longer-term implications;
- Cost pressures exceeding budget estimates;
- Non-delivery or late delivery of planned savings, including those arising from reductions in the staffing establishment;
- Impact of Welfare Reform and Pension changes;
- The costs of implementation of national policies such as free school meals, the Children and Young Peoples Bill and Council Tax Reduction Scheme exceeding the resources provided by Government; and
- Capital investment requirements and associated cost.

The financial strategy aims to mitigate a number of these risks by setting out forward plans, and the early identification of future saving proposals. Alongside this the Mi-Future programme has been designed and implemented to increase flexibility across the workforce.

### **10.3 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

### **10.4 Impact on Performance and Outcomes**

The Financial Strategy is at the heart of the way Council allocates and uses its limited resources and as such has fundamental implications for service performance and outcomes. The budget projections indicate that in 2017/18 the Council will have available in the region of £191 million for the provision of services and the pursuit of the priorities set out in the Single Midlothian Plan.

### **10.5 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.

### **10.6 Involving Communities and Other Stakeholders**

Any proposed changes in the staffing establishment arising from the elements of the financial strategy or transformation programme will be subject to meaningful consultation in accordance with the Council's Human Resources policies.

As the various elements of the Financial Strategy are developed and proposals emerge there will be meaningful consultation and engagement with those on who the proposals may impact.

### **10.7 Ensuring Equalities**

There are no equality implications arising directly from this report. As part of the development of proposals an EQIA will be prepared and for each year's budget an overarching EQIA will also be prepared encompassing the revenue budget, capital plan and service plans.

### **10.8 Supporting Sustainable Development**

There are no direct sustainability issues arising from this report.

### **10.9 IT Issues**

There are no direct IT implications arising from this report.

## **11 Summary**

The report provides an update on:-

- The Scottish Government Grant Settlement;
- The budget shortfall for 2015/16 and 2016/17;
- The initial projections for 2017/18;
- Delivery for the strands of the Financial Strategy, and in particular the Transformation Programme; and
- Reserves.

## **12 Recommendations**

Council is recommended to;

- a) Note the assumptions set out in section 4, including the increase in the assumptions made for future years pay awards.
- b) Note the projected budget shortfalls for 2015/16 through 2017/18;
- c) Note the update on delivery of the Financial Strategy.

**Date** 16 September 2014

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### **Background Papers:**