

**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 and sets out recommendations to Council to enable it to set a balanced budget and to determine Council Tax levels for 2018/19.

It includes:-

- An assessment of the 2018/19 and future years Scottish Government Grant prospects;
- Final budget projections for 2018/19 and updated budget projections for 2019/20 to 2021/22;
- A sensitivity analysis reflecting the potential impact of different pay and grant settlement scenarios;
- Details of the arrangements for the delegation of resources to the Midlothian Integration Joint Board;
- An update on the Change Programme proposed to address the projected budget shortfall in 2018/19 and to significantly reduce the budget shortfall in later years;
- 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 19 December 2017 and provided an updated assessment of projected budgets shortfalls through to 2021/22. This report provides Council with a final update on the Financial Strategy proposed for 2018/19 and update projections for later years as part of the agreed process and timetable to enable Council to determine Council Tax and set a balanced budget for 2018/19.

**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 Scottish Government's draft budget for 2018/19 was published on 14 December 2017 together with Finance Circular 5/2017 which set out the provisional grant settlement package being offered to Councils and included the individual grant figures for each Council. Alongside these the Cabinet Secretary for Finance and the Constitution set out further details of the terms of the settlement in a letter to the COSLA President and Council Leaders a copy of which was separately circulated to Councillors Parry and Winchester on 15 December 2017.

At a national level the revenue settlement included the baselining of the £130 million additional revenue funding announced at stage 1 of the Budget Bill for 2017/18 and was presented as a cash flat settlement. Within the cash flat settlement there are additional resources of £153.2 million for new burdens:-

- £52.2 million for the expansion of Early Years provision;
- £11 million to support the initial expansion of Early Years set out in the 2014 Act provisions;
- £24 million for the full year cost of Government's contribution to the 2017 Teachers' pay offer; and
- £66 million to support additional investment in social care.

When this funding for additional cost pressures is set aside the settlement published on the 14 December 2017 represented a reduction of £153 million or 1.5% in core revenue funding for Councils.

The Finance Circular also indicates that as part of the package Councils continue to have flexibility to increase Council Tax by up to 3%. Government also require local authorities to achieve a pupil/teacher ratio of 13:7 and ensure that places are provided for all probationers who require one under the Teacher Induction Scheme. However the Cabinet Secretary has indicated that in order to support delivery of this commitment the Government will work with COSLA to consider how the use of existing or additional data on unfilled posts and teacher vacancies could be better utilised to inform how delivery of this commitment is measured.

The Cabinet Secretary has also stated that in order to access all of the benefits involved, including those priorities supported by specific financial benefits, local authorities must agree to deliver all of the measures set out in the package and will not be able to select elements of the package. Any individual authority not intending to agree the offer and accept the full package of measures and benefits was requested to write to the Cabinet Secretary for Finance and the Constitution by no later than an extended deadline of Friday 26 January 2018. The Cabinet Secretary also stated that for those authorities not agreeing the offer, a revised and inevitably less favourable offer would be made. At the meeting on 19 December 2017 Council agreed that the Leader of the Council respond to the Cabinet Secretary advising that agreement to the offer and acceptance of the full package of measures and benefits was a decision for the full Council which would next meet to consider the budget on 13 February 2018.

On 23 January 2018 Government Officials issued a revision to the settlement which corrected a material error in the way the floor adjustment had been calculated along

with other more minor adjustments. This correction benefited Midlothian by £0.198 million.

At stage 1 of Parliamentary consideration of the Budget Bill the Cabinet Secretary confirmed, as part of an agreement with the Scottish Green party to support the passage of the budget bill, that Councils would benefit from an additional £170 million, £10.5 million to support inter-island ferry services and £159.5 million additional resource funding to support local government services. £34.5 million will be paid as a redetermination of grant in the current financial year and £125 million added to the grant for 2018/19. In a separate letter to the COSLA President and Council Leaders, which was separately forwarded to Councillors Parry and Winchester, the Cabinet Secretary advised that Midlothian Council would receive additional grant support of £2.630 million, £0.569 million in 2017/18 and £2.061 million in 2018/19.

Prior to the publication of the budget the Scottish Government had indicated that its future pay policy would take account of the cost of living, thereby removing the 1% pay cap. As part of the December budget announcement Government set out its pay policy for 2018/19 with a further amendment announced on 31 January 2018. The key features of the revised pay policy are as follows:-

- Lifting the pay cap by providing a guaranteed minimum increase of 3% for public sector workers who earn £36,500 or less (originally £30,000 or less);
- Continuing the requirement for employers to pay staff the real Living Wage;
- A limit of up to 2% on the increase in baseline paybill for those earning above £36,500 and below £80,000;
- Limiting the maximum pay increase for those earning £80,000 or more to £1,600.

The policy states that it acts as a benchmark for all major public sector workforce groups across Scotland including NHS Scotland, fire-fighters and police officers, teachers and further education workers. It also notes that for local government employees, pay and other employment matters are delegated to local authorities. However 2018/19 pay negotiations for local government staff will undoubtedly be informed by Government's pay policy announcement in respect of pay aspirations from the signatory trade unions who represent the local government.

As recommended to Council on 19 December 2017, the Financial Strategy now makes provision for pay awards in line with the Government's revised pay policy for 2018/19. The change announced on 31 January 2018 equates to an additional cost annual cost of £0.400 million. The Financial projections for later years set in this report are based on a provision of 2% per annum for 2019/20 to 2021/22.

Earlier projections of the budget shortfall for 2018/19 had been based on a 3.25% national reduction in grant funding, offset by the increase in Midlothian's relative share. It is now estimated that for 2018/19 Midlothian will receive a total funding package of £157.762 million of which £3.330 million is ring fenced, £2.233 million for the Attainment Scotland Fund and £1.057 for Community Justice. This leaves a core grant allocation of £154.432 million. The additional grant of £0.569 million for 2017/18 paid by way of a redetermination will increase the available reserve at 31 March 2018.

It is now estimated that the impact of the revised settlement and uplift in pay provisions would reduce the budget shortfall for 2018/19 by £4.051 million from that set out in the report on 19 December 2017.

The changes in Income Tax announced as part of the Government's budget are expected to raise £164 million rising to £220 million by 2022/23. It remains to be seen whether this is the start of a journey towards higher tax rates to help offset further cuts or whether it is a one-off decision. If it is a one-off then it will do little to ease the pressure in future years for further cuts as Governments continue in their efforts to balance budgets.

The budget documentation published on 14 December 2017 indicates that for 2019/20 the total funding available to the Scottish Government will see a 1.8% increase which is less than the 2.5% increase for 2018/19. On the basis of the information available from Government and independent sources the 2019/20 grant projections set out later in this report are now based on a central planning assumption of a 1.5% cash reduction at a national level, the same as that originally proposed for 2018/19. It also assumes that the £125 million announced on 31 January 2018 will be mainstreamed. For 2020/21 and 2021/22 the projections are based on a 2% per annum reduction at a national level. The reductions at a national level are partly offset by the impact of the relative growth in the Midlothian population.

It is stressed that the grant settlement figures for 2019/20 to 2021/22 set out table 1 are projections, the actual figures being dependant on future budget decisions taken by 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 extent of the challenge ahead for the term of the next Council and the extent to which service provision will have to be transformed.

## **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 the grant settlement offer provides 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 2018/19 and to £1,403 by 2021/22. An increase of over 3% would breach the terms of the grant settlement package and as indicated would result in a less favourable settlement although the extent of any reduction is unknown.

Given the projected budget shortfalls and the terms of the settlement the Financial Strategy incorporates a 3% increase for each year to contribute to reducing the projected budget shortfalls and Council is recommended to set a Band D Council tax of £1,283 for 2018/19 as set out in Appendix 1.

## **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. Work will continue to refine the budget projects for 2019/20 onwards with any further changes incorporated into future years Financial Strategy reports.

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

- Pay inflation for 2018/19 aligned to Government pay policy for all staff groups together with the cost of incremental pay progression. For future years pay inflation averaging 2% per annum has been assumed;
- 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 maintaining 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 maintaining pay levels for procured care services at or above the living wage;
- The impact of current demand for services;
- The 2017/18 savings targets reflecting 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;
- A provision in 2018/19 for Early Years expansion and additional investment in Health and Social Care reflecting Council's share of the monies provided in the grant settlement for these;
- The projections are based on the principal that 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 – 13 February 2018**

	<b>2018/19</b>	<b>2019/20</b>	<b>2020/21</b>	<b>2021/22</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
Cost of Services	210.907	220.408	228.651	236.532
Less: Council Tax	(46.045)	(46.645)	(47.245)	(47.845)
Less: Scottish Government Grant	(154.432)	(153.715)	(152.208)	(150.700)
<b>Budget Shortfalls</b>	<b>10.430</b>	<b>20.048</b>	<b>29.198</b>	<b>37.987</b>

The budget shortfall in 2018/19 equates 5% of the net cost of services and the projections indicate this could rise to 16% 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 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 10% for 2018/19 and has the potential to rise to 38% by 2021/22.

Whilst the projected cost of service provision, Council Tax and Scottish Government grant has been projected forward to 2021/22, the future years 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 – 13 February 2018**

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Opening Shortfall	<b>3.970</b>	<b>10.430</b>	<b>20.048</b>	<b>29.198</b>
Pay Inflation and Salary Progression	4.731	3.650	3.700	3.760
Pension Contributions	0.450	0.450	0.450	0.000
Contractual Inflation	0.718	0.637	0.571	0.652
Demographics: Care	1.040	1.040	1.040	1.040
Demographics: School Rolls	2.265	2.770	2.798	3.083
25 Hours in Primary Schools	0.090	0.000	0.000	0.000
Demand pressures: Children	0.516	0.024	0.024	0.024
School Estate Investment	0.730	1.126	0.033	0.036
Early Years Expansion	1.537	0.000	0.000	0.000
Health and Social Care new monies	0.976	0.000	0.000	0.000
Non Domestic Rates	0.132	0.135	0.138	1.142
Borrowing Costs	0.153	(0.089)	0.123	(0.007)
Scottish Government Grant	(4.740)	0.717	1.507	1.508
Council Tax Income	(1.041)	(0.600)	(0.650)	(0.650)
Full year effect of 2017/18 savings	(0.989)	(0.258)	(0.860)	(0.610)
Community Policing Teams	0.563	0.006	0.006	0.006

Newbattle Pool and Mayfield Leisure Centre	(0.542)	0.000	0.000	0.000
Other Movements	(0.129)	0.010	0.270	(1.195)
<b>Totals</b>	<b>10.430</b>	<b>20.048</b>	<b>29.198</b>	<b>37.987</b>

Since the last report further work has been undertaken to assess the financial impact of current service pressures for later years. The principal movement from the figures set out in the 19 December 2017 report are as follows.

**Table 3: Movement from 19 December 2017 to 13 February 2018**

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
<b>Shortfall 19 December 2017</b>	<b>14.081</b>	<b>25.315</b>	<b>35.375</b>	<b>45.478</b>
Pay Inflation	2.238	2.944	3.697	4.456
Early Years	1.537	1.537	1.537	1.537
Health and Social Care new monies	0.976	0.976	0.976	0.976
Scottish Government Grant	(7.912)	(10.510)	(11.079)	(14.013)
Council Tax Income	(0.441)	(0.441)	(0.441)	(0.441)
Other	(0.049)	0.227	(0.867)	(0.006)
<b>Shortfall 13 February 2018</b>	<b>10.430</b>	<b>20.048</b>	<b>29.198</b>	<b>37.987</b>

## 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 cash flat grant settlements at a national level. Otherwise all other assumptions remain as set out in section 3.

**Scenario 2.** Is a more pessimistic scenario which assumes an average pay inflation of 4% and reducing grant income as set out in section 2.

**Table 4: Sensitivity Analysis – 13 February 2018**

	2019/20	2020/21	2021/22
	£m	£m	£m
<b>Scenario 1</b>			
Central Assumption	<b>20.048</b>	<b>29.198</b>	<b>37.987</b>
Cash Flat Government Grant	(2.316)	(5.390)	(8.434)
<b>Amended Shortfall</b>	<b>17.732</b>	<b>23.808</b>	<b>29.553</b>
<b>Scenario 2</b>			
Central Assumption	<b>20.048</b>	<b>29.198</b>	<b>37.987</b>
Increased Pay Inflation	2.750	5.550	8.410
<b>Amended Shortfall</b>	<b>22.798</b>	<b>34.748</b>	<b>46.397</b>

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 Integration Joint Board (IJB). For 2017/18 the allocation was £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. The settlement included an additional £66 million for Health and Social Care to meet additional living wage costs, sleepover pressures, Carers Act commitments and the free personal care uplift. Midlothian's share of £0.976 million has been included in the proposed allocation to the IJB.

The proposed allocation now also includes £0.566 million in respect of service user transport which is being delegated from 2018/19.

The proposed Change Programme provides for the demographic cost pressures to be significantly offset with the proposed allocation of resources for 2018/19 and indicative allocations for future years estimated to be as follows:-

**Table 5: IJB allocations – 13 February 2018**

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
<b>Previous Year's Allocation</b>	37.571	39.485	40.138	39.791
Service User Transport	0.566	0	0	0
	<b>38.137</b>	<b>39.485</b>	<b>40.138</b>	<b>39.791</b>
Uplifts:				
Pay and inflation	0.681	0.653	0.653	0.653
Demographic Pressures	1.040	1.040	1.040	1.040
Additional Funding	0.976	0	0	0
	<b>40.834</b>	<b>41.178</b>	<b>41.831</b>	<b>41.484</b>
Change Programme Savings	(1.040)	(1.040)	(2.040)	(1.540)
Additional Savings Proposals	(0.309)	0	0	0
<b>Indicative Allocations</b>	<b>39.485</b>	<b>40.138</b>	<b>39.791</b>	<b>39.944</b>

Accordingly it is recommended, subject to decisions in relation to the Change Programme, that Council approve the 2018/19 allocation to the IJB of £39.485 million and advise the IJB of the updated projections for later years and that discussions continue with officers of the IJB to secure a sustainable strategy for the delivery of delegated services which can be delivered within the resource allocation. This ongoing dialogue will inform the development of both the Council's and the IJB's future years Financial Strategies.



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 a Change Programme, encompassing:-

- Delivering Excellence;
- An updated and expanded programme of transformation activity;
- The EWiM programme;
- A 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 financial challenge and Change Programme through Shaping our Future, the engagement strand of the Delivering Excellence framework. This engagement activity ran until 14 December 2017 and the feedback from this together with the feedback from the 2017/18 budget consultation is intended to help to inform 2018/19 budget decisions. Given the continuing financial challenge engagement activity continues.

An overview of feedback from the engagement activity is set out in appendix 9. A draft of this overview together with a detailed feedback report was prepared and made available to all members on 12 January 2018. The draft overview report was

also part of the agenda of the Business Transformation Steering Group on 15 January 2018.

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 allow a contribution to Reserves. Consequently, the Strategic Leadership Group have developed further proposals and also amend some of the existing proposals to take cognisance of the feedback from the engagement activity and the impact of the grant settlement.

A draft of the updated proposals representing the Strategic Leadership Group's assessment of the most appropriate solution to secure a balanced budget at that point in time was presented to the Business Transformation Steering Group on 15 January 2018 where BTSG members noted the proposals and noted that they would form part of the final proposals presented to Council on 13 February 2018.

The Change Programme presented today, as set out in Appendix 8, remains the same as that presented to BTSG and has not been amended as a consequence of the increase in the settlement announced on 31 January 2018. This takes cognisance of the continuing challenge for later year's budgets though members may wish to take account of the revised settlement in finalising their proposals for 2018/19.

## **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 the decision of Council on 19 December 2017 in respect of property rationalisation. This results in the removal of the previously reported savings target for the Services to Communities Review which are now reflected in the budget shortfalls set out in section 5.

Table 6 sets out the savings targets for the remainder of the existing programme which are £1.167 million for 2018/19 rising to £1.502 million by 2021/22. Other than the change 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 – 13 February 2018**

	<b>2018/19</b>	<b>2019/20</b>	<b>2020/21</b>	<b>2021/22</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
Children's Services	0.000	0.335	0.335	0.335
Education	0.127	0.127	0.127	0.127
Health and Social Care	1.040	1.040	1.040	1.040
<b>Totals</b>	<b>1.167</b>	<b>1.502</b>	<b>1.502</b>	<b>1.502</b>

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

**Table 7: Additions to Transformation Programme – 13 February 2018**

	<b>2018/19</b>	<b>2019/20</b>	<b>2020/21</b>	<b>2021/22</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
Entrepreneurial Council	0.410	1.968	3.178	4.988
Services with Communities	0.000	0.200	0.300	1.300
Shared Services	0.025	0.085	1.085	2.085
Digital Led Transformation	0.050	0.100	0.200	0.700
Integrated Service Support	0.480	0.980	0.980	0.980
Workforce Planning	0.728	1.210	1.360	1.450
Health and Social Care	0.309	1.349	3.389	4.929
<b>Additions to Programme</b>	<b>2.002</b>	<b>5.892</b>	<b>10.492</b>	<b>16.432</b>

Appendix 2 sets out those items included in the above strands where a decision is sought from Council today to allow the changes to be implemented. Appendix 3 summarises the proposals in respect of later years which are simply for noting at this point. Fuller details for both are set out in the Change Programme at Appendix 8. Otherwise the remaining savings targets set out in tables 6 and 7 are predicated on the outcomes of reviews and future 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 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 before the summer recess. This will enable the full implications of the Learning Estate Strategy and other emerging investment pressures to be fully considered before presenting a revised Capital Strategy and Plan.

Borrowing to fund investment in the Council's Asset base is made by way of advances from the Council's internal Loans Fund with the advances repaid from the revenue accounts over a predetermined period, much like a conventional mortgage. The Loans Fund finances these advances by external borrowing, principally from the Public Works Loan Board (PWLb). This activity is governed by the Treasury Management and Investment Strategy approved by the Council each year at the

same time that the budget is approved. As part of this activity a review of the Loans Fund accounting arrangements is being undertaken which includes an assessment of the period over which Loans Fund advances are projected to be repaid. At this time a savings target of £0.500 million has been attached to the review and reflected in the 2018/19 proposed budget with the final outcome of the review expected to be reflected in the both the revised Capital Strategy and Plan.

The latest projections for the General Fund Reserve are set out later in this report. An updated 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 updated projections summarised below.

**Table 8: Operational Savings – 13 February 2018**

	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	0.470	0.520	0.570	0.620
Cost Reductions	0.330	0.440	0.525	0.530
Workforce Reductions	0.570	1.226	1.256	1.446
<b>Operational Savings</b>	<b>1.370</b>	<b>2.286</b>	<b>2.601</b>	<b>2.896</b>

A breakdown is set out in appendix 4.

## 8.6 Savings

The budget proposals presented to Council on 10 October 2017 include a number of Service Reviews and specific policy cost reductions. The updated proposals, incorporating the additional proposals from the Senior Leadership Group are:-

**Table 9: Policy Saving Proposals- 13 February 2018**

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
Service Reviews	1.262	1.912	2.812	3.206
Policy Cost Reductions	5.078	6.775	7.025	7.275
<b>Policy Saving Proposals</b>	<b>6.340</b>	<b>8.687</b>	<b>9.837</b>	<b>10.481</b>

Appendix 5 sets provided a summary of the proposals with fuller details set out in the Change Programme at Appendix 8.

## 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. In addition the proposals from the Senior Leadership Group provide for the generation of additional income from fees and charges of £0.100 million from 2018/19. Appendix 6 sets out the detailed proposals for fees and charges for Council approval.

## 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 with the resultant 2018/19 service budgets detailed in Appendix 7.

**Table 10: Financial Strategy 2018/19 to 2021/22 – 13 February 2018**

	2018/19	2019/20	2020/21	2021/22
	£m	£m	£m	£m
<b>Budget Shortfall Table 1</b>	<b>10.430</b>	<b>20.048</b>	<b>29.198</b>	<b>37.987</b>
<b>Less: Change Programme</b>				
<b>Transformation Programme 8.2</b>				
- Existing Programme	(1.167)	(1.502)	(1.502)	(1.502)
- Additions to Programme	(2.002)	(5.892)	(10.492)	(16.432)
<b>Total Transformation Programme</b>	<b>(3.169)</b>	<b>(7.394)</b>	<b>(11.994)</b>	<b>(17.934)</b>
<b>Asset Management 8.3</b>	<b>(0.000)</b>	<b>(0.288)</b>	<b>(0.288)</b>	<b>(0.288)</b>
<b>Loan Charges 8.4</b>	<b>(0.500)</b>	<b>(0.500)</b>	<b>(0.500)</b>	<b>(0.500)</b>
<b>Operational Savings 8.5</b>	<b>(1.370)</b>	<b>(2.286)</b>	<b>(2.601)</b>	<b>(2.896)</b>
<b>Savings Options 8.6</b>				
- Policy Cost Reductions	(5.078)	(6.775)	(7.025)	(7.275)
- Service Reviews	(1.262)	(1.912)	(2.812)	(3.206)
<b>Total Policy Savings</b>	<b>(6.340)</b>	<b>(8.687)</b>	<b>(9.837)</b>	<b>(10.481)</b>
<b>Fees and Charges 8.7</b>	<b>(0.180)</b>	<b>(0.240)</b>	<b>(0.280)</b>	<b>(0.300)</b>
<b>Less:</b>				
<b>Council Tax Increase of 3%</b>	<b>(1.274)</b>	<b>(2.569)</b>	<b>(3.884)</b>	<b>(5.218)</b>
<b>Sub Total</b>	<b>(2.403)</b>	<b>(1.916)</b>	<b>(0.186)</b>	<b>0.370</b>
<b>Transfer to Reserves</b>	<b>2.403</b>	<b>1.916</b>	<b>0.186</b>	<b>0.000</b>
<b>Remaining Budget Gap</b>	<b>0.000</b>	<b>0.000</b>	<b>0.000</b>	<b>0.370</b>

The Change Programme summarised above secures a balanced budget for 2018/19, and subject to amendments would secure an increase in General Fund reserves. Again subject to the impact of amendments the projections indicate a sustainable financial position through to 2020/21.

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. The next iteration of the Financial Strategy, beginning the development of the 2019/20 budget will be presented to Council in June 2018. Work will also be required to review and bring forward further proposals in respect of the following areas:-

- 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;
- Workforce, recognising that employee costs are by far the largest element of the budget.

In finalising the budget proposals for 2018/19 I have, as Section 95 Officer, sought 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 have been 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 which 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. The timetable agreed by Council on 27 June 2017 provided for the determination of the 2018/19 budget and Council Tax levels at today's Council meeting.

**Table 11: Timetable – Key Events**

Date	Event	Action
13 February 2018	Council	<ul style="list-style-type: none"> <li>• Consideration of update report, reflecting grant settlement.</li> <li>• Finalisation of Change Programme and savings proposals.</li> <li>• Recommendations to set Council Tax and determine a budget for 2018/19.</li> </ul>

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 today's meeting members will be required to disclose before the report is considered 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, including the impact of the redetermination announced on 31 January 2018 is set out in the Financial Monitoring 2017/18 – General Fund Revenue report on today's agenda.

The projected uncommitted General Fund Reserve at 31 March 2018 is £3.984 million. This uncommitted reserve is marginally below the minimum prudent level required to provide a contingency.

A prudent level of uncommitted reserves required 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 is seen to be between 2% and 4% of net expenditure which equates to between approximately £4 million and £8 million. The Change Programme proposals set out earlier in this report, if approved in full, would result in a reinstatement of available reserves of £2.403 million with a resultant available contingent reserve of £6.387 million which would equate to approximately 3% of net expenditure.

Table 12 summarises the General Fund Reserve position.

**Table 12: Available General Fund Reserve 31 March 2018 – 13 February 2018**

	<b>£million</b>
<b>General Fund Balance at 31 March 2018</b>	<b>8.763</b>
<i>Earmarked for specific purposes</i>	
• Earmarked for Council Transformation	(3.532)
• Devolved School Management	(1.247)
<b>Available Contingent Reserve at 31 March 2018</b>	<b>3.984</b>
Reinstatement in 2018/19	2.403
<b>Available Contingent Reserve</b>	<b>6.387</b>

In addition the unallocated balance on the Capital Fund at 31 March 2018 is projected to be £11.066 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 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 bring forward and implement a comprehensive Change Programme is critical to enable Council to address the projected budget gaps and in securing financial sustainability for the continued delivery of services.

The severity of the challenge is such that Council will require to approve a range of proposals today 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 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**

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. This engagement activity ran until 14 December 2017. The feedback from this activity together with the feedback from the 2017/18 budget consultation is intended to help to inform 2018/19 budget decisions. Given the continuing financial challenge engagement activity continues.

An overview of feedback from the engagement activity is set out in appendix 9. A draft of this overview together with a detailed report was prepared and made available to all members on 12 January 2018 and the draft overview report was also on the agenda for the Business Transformation Steering Group on 15 January 2018.

In addition, there has been and 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 a further update at the Joint Consultative Group meeting on 6 February 2018.

## **12.7 Ensuring Equalities**

The Financial Strategy and the Change Programme proposals which support financial sustainability have 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 Change Programme proposals 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.

Updated copies of the individual assessments have been published alongside this report on the Committee Management System (CMIS) section of the Council website and an updated overarching EqIA is also set out in appendix 10. 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. The mitigating actions will form part of the implementation of changes when approved.

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 the 2018/19 and future years Scottish Government grant prospects;
- Final budget projections for 2018/19 and updated budget projections for 2019/20 to 2021/22;
- A sensitivity analysis reflecting the potential impact of different pay and grant settlement scenarios;
- Details of the arrangements for the delegation of resources to the Midlothian Integration Joint Board;
- An update on the Change Programme proposed to addressing the projected budget shortfall in 2018/19 and to significantly reduce the budget shortfall in later years;
- 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 for 2018/19 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) In line with the provisions of the Grant Settlement package set a Band D Council Tax of £1,283 for 2018/19 as set out in appendix 1;
- d) Note the continuing uncertainties and the potential impact as outlined in the differing scenarios as set out in section 6;
- e) Consider the Change Programme elements proposed by the Strategic Leadership Group as set out in section 8 and:-
  - I. Approve the savings proposals associated with the additions to the Transformation Programme as set out in appendix 2;
  - II. Note the savings proposals associated with the additions to the Transformation Programme in later years as set out in appendix 3;
  - III. Note the operational savings summarised in appendix 4;
  - IV. Approve the service review and policy savings proposals as set out in appendix 5;
  - V. Note the additional income anticipated from fees and charges as set out in section 8.7 and approve the detailed charges set out in appendix 6;
- f) Approve the allocation of £39.485 million to the Midlothian Integrated Joint Board for 2018/19 in respect of delegated services;
- g) Subject to any amendments for the decisions taken at items c) and e) I and IV and f) approve the resultant 2018/19 service budget as set out in appendix 7, including a transfer to reserves of £2.403 million;
- h) In considering the recommendations also consider the contents of the overview of feedback from engagement activity set out in appendix 9 and the overarching EQIA set out in appendix 10;
- i) Otherwise note the contents of the report.

Date 5 February 2018

### Report Contact:

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Appendix 1 - Council Tax

Appendix 2 - Savings decisions – Additions to Transformation Programme

Appendix 3 - Later Years changes

Appendix 4 - Operational savings  
Appendix 5 - Policy Proposals  
Appendix 6 - Fees and Charges  
Appendix 7 - Proposed 2018/19 Service Budgets  
Appendix 8 - Change Programme  
Appendix 9 - Engagement Feedback  
Appendix 10 - Overarching EQIA

## MIDLOTHIAN COUNCIL

## Council Tax for Financial Year 2018/19

This statement gives details of the 2018/19 Council Tax payable in respect of a chargeable dwelling in each of the valuation bands specified in Section 74(2) of the Local Government Finance Act 1992 determined in accordance with Section 74(1) of the Act (as amended)

**Based on Band D Council Tax of £1,283.**

Band	Range of Values		Band D Proportion	Council Tax £
	From £	To £		
<b>A</b>	-	27,000	240/360	855.33
<b>B</b>	27,001	35,000	280/360	997.88
<b>C</b>	35,001	45,000	320/360	1,140.44
<b>D</b>	45,001	58,000	360/360	1,283.00
<b>E</b>	58,001	80,000	473/360	1,685.72
<b>F</b>	80,001	106,000	585/360	2,084.87
<b>G</b>	106,001	212,000	705/360	2,512.54
<b>H</b>	212,001	upward	882/360	3,143.35

## REVENUE BUDGET 2018/19 SUMMARY

<b>Service Function</b>	<b>Budget 2018/19 £</b>
Management and Members	1,868,156
<u>Education Communities and Economy</u>	
Childrens Services	15,237,667
Communities and Economy	3,226,589
Education	89,662,858
<u>Health and Social Care</u>	
Adult Social Care	39,484,938
Customer and Housing Services	11,199,784
<u>Resources</u>	
Commercial Services	13,318,662
Finance and Integrated Service Support	11,425,333
Properties and Facilities Management	13,193,746
Lothian Valuation Joint Board	550,550
Centrally Held Budget Provisions	717,900
Non Distributable Costs	1,338,437
<b>GENERAL FUND SERVICES NET EXPENDITURE</b>	<b>201,224,620</b>
Loan Charges	7,060,000
Investment Income	(371,475)
Council Transformation Programme savings targets	(3,631,224)
Allocations to HRA, Capital Account etc.	(4,934,180)
<b>NET EXPENDITURE</b>	<b>199,347,741</b>
Enhancement of Reserves	(2,403,259)
Scottish Government Grant	154,432,000
Council Tax	47,319,000
<b>TOTAL FUNDING</b>	<b>199,347,741</b>