ITEM 4

FINANCIAL STRATEGY 2013/14 – 2017/18

Report By Chief Financial Officer

SCOTTISH BORDERS COUNCIL

7 February 2013

1 PURPOSE AND SUMMARY

1.1 **This report seeks approval for the financial strategy for the Council covering the period 2013/14 – 2017/18.**

1.2 The Council aims to provide the best possible services within the resources available.

This requires a financial strategy which:-

a) raises the funds required by the Council to meet approved service levels in the most effective manner;

b) manages the effective deployment of those funds in line with the Council's corporate objectives and approved service plans; and,

c) provides stability in resource planning and service delivery.

This strategy addresses a number of important issues which must be considered in setting the budget for the coming year. For the first time a 5 year financial plan has been developed to assess the likely level of resources available over that period and the budgetary adjustments that will be required to ensure the Council's financial plans remain prudent and sustainable in the longer term. Firm figures are only available from the Finance settlement for 2013/14 and 2014/15 and consequently it is recognised that the financial strategy will be adapted over time to respond to changing circumstances. The strategy refines the approach to setting council balances using a risk based approach first adopted as part of the 2012/13 budget process. The risk register has been fully reviewed in compiling the updated financial strategy and a recommendation is made regarding the level of unallocated balances.

2 RECOMMENDATIONS

2.1 **It is recommended that Council approves the financial strategy for 2013/14 – 2017/18 as set out in section 3.1 and agree to maintain unallocated balances of £5.614m in 2013/14 as set out in the risk register in appendix 1.**

3 Financial Strategy 2013/14 - 2017/18

3.1 Background

The financial strategy set out in this paper recognises the continuing difficult economic outlook. Informed opinion has concluded that the current recession will last longer and bite deeper than previously envisaged. The economic outlook has a direct bearing on public expenditure with the need for tight fiscal constraint to be maintained for the foreseeable future. This requires a financial strategy which raises the funds required by the Council to meet approved service levels in the most effective manner, manages the effective deployment of those funds in line with the Council's corporate objectives and approved service plans and provides stability in resource planning and service delivery.

This strategy also recognises the need to ensure that the Council's budget is targeted so that it:-

- provides the most effective stimulus to the wider economy,
- protects those who are most vulnerable in society,
- recognises the need to continue providing good value for money.

The strategy reflects the Council's duty to set a prudent, sustainable budget, to invest in core services, to work effectively with partner organisations - assisting them in the delivery of their strategic objectives where possible, to protect council tax payers and ensure service charges remain as affordable as possible for residents of the Scottish Borders.

The recommended high level financial strategy to be followed over the next five years is therefore to:-

- **freeze council tax in each year of the budget;**
- **set a prudent, sustainable budget in line with available resources;**
- **continue to invest in infrastructure through a sustainable capital programme financed by £21.3m loans charges per annum;**
- **provide a £13m loan facility to registered social landlords operating in the Scottish Borders as a stimulus to house building and wider economic development;**
- **maximise income while keeping fees charged to service users at an affordable level;**
- **invest in business transformation and efficiency projects in each year of the five year plan to deliver long term financial savings and service benefits, and,**
- **maintain unallocated reserves of £5.614m for 2013/14 in line with the assessed risk register.**

3.2 Aggregate External Finance

It is assumed the full level of AEF, estimated at £197.7m, after adjusting for the transfer of police and fire resources and excluding specific grants, will be deployed in setting the 2013/14 revenue budget. This level of funding is conditional upon council tax again being frozen at 2007/08 levels. AEF in 2014/15 is projected to be £197.3m.

3.3 Council Tax

The financial strategy assumes that Council will approve a freeze in the council tax, setting band D equivalent of £1,084 for each of the next five years. All other council tax bands vary as a set proportion of the band D figure. The Scottish Borders council tax product, following a review of the properties, collection rates and levels of bad debt provision, is estimated as £50.926m in 2013/14 and £51.126m in 2014/15. Over the 5 year period, the council tax product derived from increasing numbers of homes (partly resulting from council backed investment in house building and the positive impact of the Borders Railway) is expected to increase.

3.4 Council Tax – 2nd Homes

Council has a policy of applying a 10% discount to long term empty dwellings and 2nd homes which is the minimum discount allowable under the Council Tax (Discount for Unoccupied Dwellings) (Scotland) regulations 2005. This provides a budget of £0.715m per annum which is ring fenced for affordable housing in the Scottish Borders. The Government has recently consulted on changes to these regulations and these will be submitted to parliament in due course. The consultation raises the prospect for the Council to levy a discretionary surcharge of up to 100% of council tax on second homes in future. The financial strategy reflects the current practice of allowing a 10% discount for 2nd homes in the area.

3.5 Reserves

3.5.1 The Council maintains a number of funds and balances which are reported to elected members at regular intervals during the financial year. Table 1 below shows the projected balance on each fund at 1 April 2013.

Table 1 Funds and Balances	**1 April 2013**
	(Estimated)
	£'000
Statutory Funds	
Corporate Property Repairs and Renewals Fund	28
Plant and Vehicles Renewals Fund	2,263
Insurance Fund	1,398
Capital Fund Excl Developer Contributions	3,367
General Fund – Earmarked	
Devolved School Management	740
Specific Departmental Reserves	1,904
Issues identified in this report	1,615
General Fund – Non-Earmarked	5,614
Total	16,629

The Council holds reserves in order to manage identified risks, smooth uneven cash flows and provide a contingency against unforeseen circumstances. The existence and management of reserves is a fundamental aspect of any sound financial strategy. The financial strategy and the associated reserves position is subject to scrutiny by the Council's auditors and other external agencies.

3.5.2 On 9th February 2012 the Council agreed to adopt a Corporate Financial Risk Register (an updated version of which is attached at Appendix 1) as the basis for setting reserve levels in 2012/13 and future years. This approach considers issues including the failure by managers to enact effective budgetary control, severe weather events, the economic downturn, potential contractual claims and unplanned emergencies in deriving an appropriate level of unallocated balances.

3.5.3 A review of the major risks facing the Council has been undertaken by senior finance officers and these are shown in the risk register in appendix 1. Following this exercise the level of un-allocated general fund balances is now directly informed by an assessment of the risks facing the Council.

3.5.4 The risk based approach it is considered better reflects the risks inherent in setting the revenue budget, the reasons why reserves are held in the first place, the scale and complexity of the organisation and also provides greater transparency with regard to the level of balances held.

3.5.5 There are, in addition, a number of issues which will have a bearing on the level of unallocated balances and which require to be considered in an updated analysis of unallocated balances.

Municipal Mutual Insurance

3.5.6 MMI is an insurance company limited by guarantee and not having a share capital. The Company suffered substantial losses between 1990 and 1992 and these losses reduced MMI's net assets to a level below the minimum regulatory solvency requirement. In September 1992 MMI ceased to write new, or to renew, general business insurance. A contingent Scheme of Arrangement under Section 425 of the Companies Act 1985 became effective on 21 January 1994. The former Borders Regional Council was a creditor of MMI, and as such SBC became a Scheme Creditor under the Scheme of Arrangement in 1996.

The majority of claims related to occupational disease claims, mainly mesothelioma (asbestos). At the time it was thought that MMI would be able to "run off" its remaining liabilities and continue to pay agreed claims in full. It was anticipated that this process would continue for at least 20 years. In the event that this could not continue, a "trigger event" would be initiated and Scheme Creditors would have to pay a claw back.

In anticipation of a possible trigger event but in the hope that a solvent run off would still be possible, the Council noted a contingent liability in the 2011/12 accounts. It is understood however that a solvent run off of MMI is no longer anticipated and that this contingent liability will now crystallise. Consequently it will be necessary to make a provision of £0.388m in the accounts to fund a claim against SBC as an MMI creditor. A full report on this issue was considered by Council on the 31 January 2013.

Winter

3.5.7 Members will recall that £0.565m of the general fund reserves have previously been allocated to winter. Early indications are that expenditure this year in excess of budget will require this funding to be drawn down to support winter thereby reducing the unallocated balance and that the sums noted will require a provision in the accounts.

Both these items will be reflected in the 9 month monitoring report to be submitted to Executive on the 19 February 2013.

Drawdown of balances to support the revenue and capital budget.

3.5.8 The 5 year revenue plan assumes the drawdown of £0.2m in 2014/15 from reserves to fund early retiral / voluntary severance. This will assist the Council in delivering ongoing reductions in the pay bill. The capital plan also assumes that £0.45m will be allocated from reserves upon receipt of external match funding for the Selkirk High School synthetic pitch.

Unallocated balances

3.5.9 Given the calls on reserves noted above, issues identified in the risk register and risks inherent in setting the revenue budget, members are recommended to maintain an unallocated general fund equivalent to £5.614m) in 2013/14. The unallocated balance projected at the 31st March, before adjustments for police and fire reserves, is sufficient to cover 58% of the risks identified in the risk register should they materialise.

Technical Adjustments

3.5.10 It should be noted that the projected balances exclude any technical adjustments which are required as part of year end accounting processes. In 2011/12 these adjustments were broadly neutral and did not materially affect the level of reserves but it is possible that future adjustments may make a material impact, positively or negatively, on the final balances.

3.6 Treasury Management Strategy 2013/14

This forms a key aspect of the Council's overall financial management strategy. The Treasury Management Strategy, submitted elsewhere on the agenda for approval, sets out the arrangements for financing the Council's capital investment plan, the associated prudential indicators, how the treasury function will be organised, and an investment strategy setting out the parameters governing how the Council's investments are to be managed.

3.7 Capital Investment

The updated 10 year capital plan and an accompanying report are also submitted elsewhere on the agenda. The financial strategy aims to ensure capital borrowing is within prudential borrowing limits and sustainable in the longer term. In this regard it is important to recognise the capital investment decisions taken now have long term borrowing implications and these have the potential to place an undue burden on future tax payers. The draft revenue budget sets loans charges associated with capital borrowing over the next 5 years at £21.3m per annum. This will be kept under review in light of the prevailing economic condition and opportunities for debt re-structuring. The Council has significant revenue resources tied up in capital assets and work will continue to identify surplus property for disposal in order to reduce revenue running costs and deliver capital receipts.

3.8 Loan facility to Borders based Registered Social Landlords (RSL's).

Council agreed the principle of lending to Borders Based RSL's at its meeting of 15 December 2011 and a report elsewhere on this agenda now seeks permission to provide a £13m loan facility to 3 RSL's. It is envisaged that these security backed loans will assist the development of up to 163 additional affordable housing units which have been previously identified and prioritised via the Council's Strategic Housing Investment Plan (SHIP). This initiative if approved will also require Scottish Government "consent to borrow" and will provide a major policy stimulus to the local economy.

3.9 Bad Debts

Income collection, including council tax, may be adversely affected by the difficult economic conditions The budget assumes that the contribution to the bad debt provision will remain at £0.125m for sundry debt and £0.715m for council tax for 2013/14 and this will be kept under review over the five year period.

3.10 Risks presently un-quantified in the Revenue budget

There are two further specific areas of concern with regard to risks in the budget process for 2013/14 onwards.

3.10.1 Welfare Reform

The implications of Welfare Reform have not been quantified in the financial model due to the lack of specific information with respect to the complex nature of Government's proposals. While longer term proposals will be far reaching, the immediate effects on the Council's Finances in 2013/14 are thought at this stage to be limited, beyond the immediate issues associated with Council tax benefit and the implementation of universal credit set out for 2013/14 in the 5 year financial model.

3.10.2 Auto Enrolment

A second area of unfunded risk relates to Auto Enrolment in the pension fund which is due to commence in July 2013. It is not possible at this stage to quantify the effects of auto enrolment with any degree of certainty due to the diverse nature of posts across the council. A general estimate assumes that 50% of staff not current enrolled may elect to join. The impact of personal circumstances on the decisions of individuals to enrol or opt out of the pension scheme will have a material bearing on final costs. If all SJC staff not presently enrolled choose the join the pension scheme an additional cost to the council of £1.1m per annum has been provisionally quantified. A decision to defer auto enrolment for all staff and implement provisions relating to transitional arrangements for auto enrolment will defray this risk. It is understood this is the approach now being adopted by the majority of Scottish Local Authorities and a report recommending a course of action will be brought to members in due course. Welfare Reform and Auto Enrolment are both areas where a robust policy with respect to reserves will assist the council in managing residual risk.

3.11 Overall approach to cost reduction and service reviews

It is evident that the Council faces ongoing cost pressures in its revenue budget and this will require a focus on cost control, an innovative approach to business transformation, robust change management processes and a sustained drive to improve efficiency. The need to develop a longer term financial plan early in the new administration was signalled in the financial strategy approved by Council on the 9 February 2012. In response a five year financial outlook model has now been developed by the Council Management Team. The background to this model, its main features, and the challenges to be addressed, were documented in a report to Council on the 13th December 2012. At that meeting members agreed to adopt the model as the basis for the Council's 5 year revenue plan 2013/14 - 2017/18 and approved an initial set of revenue savings for 2013/14 for budget consultation. These initial savings, along with a range of other business transformation proposals covering the next 5 financial years, and proposals for growth in the budget to meet a range of pay, inflation, demographic and other service pressures are now included in the Administration's five year revenue plan. This is included for approval elsewhere on the Council agenda.

3.12 Staffing

At a cost of around £150m per annum pay and associated on-costs represent the largest single element of council expenditure. Public sector pay policy continues to be subject to ongoing restraint and the financial plan assumes modest cost of living increases of 1% in 2013/14, 1% in 2014/15 rising to 2% for the remaining 3 years of the financial plan. The ability to adapt terms and conditions to reflect modern working practices and down size the Council's work force in response to continuing financial pressures is a key tool in mitigating future cost pressures. In order to assist with this strategy, the financial plan provides £4.6m over the 5 year period for early retrial/voluntary severance.

3.13 Social Work pressures

The 5 year financial plan makes significant provision from year one with a recurrent additional resources of £1.384m allocated to fund the deficit evident in the Social Work budget in the current year. Members will recall this issue was reported to the Council Executive in the month 6 monitoring report along with an action plan to bridge the projected financial deficit. The provision in the financial plan represents the residual unfunded gap.

3.14 Local Government Pension Fund

The 2011 triennial revaluation of the pension fund by the Council's actuary Barnett Waddingham maintained employer's superannuation contributions at 18% for the 3 year period to 31 March 2014. Overall however the funding level dropped marginally to 95.7%. The long term view is that the fund remains in a healthy state with the deficit recovery period to return to 100% funding remaining at 12 years. It should be noted that the Council's employer contributions are relatively low compared to the majority of Scottish Local Authority Pension funds and the financial plan recognises that there may be a requirement for these contributions to increase in future.

4 IMPLICATIONS

4.1 Financial

There are no additional financial implications associated with this report, its content referring specifically to the financial strategy of the Council and the associated revenue and capital budgets and reserve levels.

4.2 Risk and Mitigations

(a) The existence of appropriate balances is a fundamental aspect of sound governance and effective stewardship. There is therefore a risk to the Council from not having an appropriate financial strategy underpinned by cash backed reserves which will be mitigated by approval of this report.

(b) If the identified risks were to materialise, without an appropriate level of reserves, Council would be required to identify alternative funding, possibly at short notice, through reduced services, asset disposals, increased charges or additional unbudgeted borrowing.

4.3 Equalities

There are no adverse equality implications arising from this report.

4.4 Acting Sustainably

There are no economic, social or environmental effects arising directly from this report.

4.5 Carbon Management

There are no effects on carbon emissions.

4.6 Rural Proofing

There are no implications that would compromise the Council's rural proofing policy.

4.7 Changes to Scheme of Administration or Scheme of Delegation

There are no changes required to either the Scheme of Administration or the Scheme of Delegation

5 CONSULTATION

5.1 The Head of Legal and Democratic Services, the Head of Audit and Risk and the Clerk to the Council have been consulted in the preparation of this report.

Approved by

David Robertson
Chief Financial Officer

Author

Name	Designation and Contact Number
David Robertson	01835 825012

Background Papers:
Previous Minute Reference: Council Report 9 February 2012 and 13 December 2012

Note – You can get this document on tape, in Braille, large print and various computer formats by contacting the address below. Finance can also give information on other language translations as well as providing additional copies.

Contact us at: Debbie Collins, Financial Services Manager, Scottish Borders Council, Council Headquarters, Newtown St Boswells, and Melrose, TD6 0SA.
Telephone – 01835 825018. Fax – 01835 825011. e-mail – debbie.collins@scotborders.gov.uk