ITEM 5

FINANCIAL STRATEGY 2014/15 – 2018/19

Report By Chief Financial Officer

SCOTTISH BORDERS COUNCIL

6 February 2014

1 PURPOSE AND SUMMARY

1.1 This report seeks approval for the financial strategy for the Council covering the period 2014/15 – 2018/19.

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.

1.3 This strategy addresses a number of important issues which must be considered in setting the budget for the coming year and indicative budgets for the following 4 years. A 5 year financial plan has been rolled forward to assess the likely level of resources available over that period and the budgetary adjustments that will be required to ensure the Council’s finances remain prudent and sustainable in the longer term. Firm figures are only available from the Finance settlement for 2014/15 and consequently it is recognised that the financial strategy will be adapted over time to respond to changing circumstances. The strategy uses an approach based on a financial risk register to set unallocated balances contingency underpinning the 5 year plan. This has informed the updated financial strategy and the recommended level of unallocated balances.

2 RECOMMENDATIONS

2.1 It is recommended that Council approves the financial strategy for
2014/15 – 2018/19 as set out in section 3.4 and agree to maintain unallocated balances of £6.3M in 2014/15 as set out in the risk register in appendix 1. The financial strategy seeks 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 £20.8m loans charges per annum;
- provide support to an Affordable Housing Investment Programme of up to £18.8m for the delivery of 200 units;
- maximise income while keeping fees charged to service users at an affordable level;
- continue to invest in business transformation and efficiency projects to deliver long term financial savings and service benefits, and,
- maintain unallocated reserves of £6.313m for 2014/15 in line with the assessed risk register.
Financial Strategy 2013/14 - 2017/18

3 Background

3.1 The financial strategy set out in this paper recognises the continuing pressure on public sector funding. 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.

3.2 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.

3.3 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.

3.4 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 £20.8m loans charges per annum;
- provide support to an Affordable Housing Investment Programme of up to £18.8m for the delivery of 200 units;
- maximise income while keeping fees charged to service users at an affordable level;
- continue to invest in business transformation and efficiency projects to deliver long term financial savings and service benefits, and,
- maintain unallocated reserves of £6.313m for 2014/15 in line with the assessed risk register.

4 FUNDING

4.1 Aggregate External Finance

It is assumed the full level of AEF, estimated at £198.906m, excluding specific grants, will be deployed in setting the 2014/15 revenue budget. This level of funding is conditional upon council tax again being frozen at 2007/08 levels.

4.2 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 £51.126m in 2014/15 and £51.626m in 2015/16. 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.

**4.3 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 Council has committed to providing support to an Affordable Housing Investment programme of £18.8m. It is proposed as part of the affordable housing development programme, for up to 200 units, that funding of £3.3m from 2nd homes council tax is used to offset the land acquisition costs over the programme delivery period. The Government issued new guidance on the changes to these regulations in May 2013 which allows the Council to levy a discretionary surcharge of up to 100% of council tax on second homes in future. The financial strategy however reflects the current practice of allowing a 10% discount for 2nd homes in the area.

**5 RESERVES**

**5.1 Reserves**

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 2014.

<table>
<thead>
<tr>
<th>Table 1 Funds and Balances</th>
<th>1 April 2014 (Estimated) £’000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Statutory Funds</strong></td>
<td></td>
</tr>
<tr>
<td>Corporate Property Repairs and Renewals Fund</td>
<td>0</td>
</tr>
<tr>
<td>Plant and Vehicles Renewals Fund</td>
<td>2,021</td>
</tr>
<tr>
<td>Insurance Fund</td>
<td>1,340</td>
</tr>
<tr>
<td>Capital Fund Excl Developer Contributions</td>
<td>3,131</td>
</tr>
<tr>
<td><strong>General Fund – Earmarked</strong></td>
<td></td>
</tr>
<tr>
<td>Devolved School Management</td>
<td>880</td>
</tr>
<tr>
<td>Specific Departmental Reserves</td>
<td>3,032</td>
</tr>
<tr>
<td>Allocated reserves</td>
<td>4,065</td>
</tr>
<tr>
<td><strong>General Fund – Non-Earmarked</strong></td>
<td>6,313</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>20,782</td>
</tr>
</tbody>
</table>

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.

**5.3** A Corporate Financial Risk Register (an updated version of which is attached at Appendix 1) has been used as the basis for setting reserve...
levels in 2014/15 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.

5.4 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. The risk based approach it is considered 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 appropriate transparency with regard to the level of balances held.

5.5 **Unallocated balances**

Given the 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 £6.313m in 2014/15. The unallocated balance projected at the 31st March 2014 is sufficient to cover 63% of the risks identified in the risk register should they materialise and reflects 2.5% of the 2014/15 revenue budget.

5.6 **Technical Adjustments**

It should be noted that the projected balances exclude any technical adjustments which are required as part of year end accounting processes. In 2012/13 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. It should be noted that the 2013/14 figures included £3.032m of balances earmarked for use in 2014/15 and the current year projected balances will increase if budgets are earmarked to future years during the course of 2013/14.

6 **FINANCIAL RISKS**

6.1 A number of issues have a bearing on the level of unallocated balances has been identified in the financial risk register set out in appendix 1 in determining the level of unallocated reserves at £6.313m.

6.2 **Winter**

Members will recall that £0.565m of the general fund reserves have previously been allocated to winter as part of the final revenue outturn for 2012/13. Currently the monitoring projects that expenditure this year will be within budget and barring a significant deterioration in the weather between now and the 31 March will not require a draw down to support winter. It is therefore proposed that this balance be rolled forward to support winter in 2014/15. If weather worsens between now and the 31 March clearly the Council may need to call on these reserves.

6.3 **Drawdown of balances to support the revenue and capital budget**.

The 5 year revenue plan assumes the drawdown of £1.2m in 2014/15 from reserves, with £1m to be repaid over two years, to fund early
retiral / voluntary severance and the transition to new terms and conditions. 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.

7 TREASURY AND CAPITAL

7.1 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.

7.2 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 £20.8m per annum, a reduction of £0.5m from the previous budget position of £21.3m. A review of loan charges has been undertaken which has identified a permanent reduction of £0.5m commencing in 2014/15 can be afforded as long as future capital borrowing is controlled in a sustained and prudent manner. The review assumes an increase in currently approved levels of capital borrowing of £10m in each of the next three years and then reducing to an additional £7.5m in 17/18 and £5m in subsequent financial years. The analysis undertaken to date assumes that the strategy of deferring new borrowing and instead funding capital expenditure from surplus cash flow and temporary loans can continue. A further one off contribution of £1m from loans charges in 2013/14 to assist with the budget process in 2014/15 was approved by the Executive on the 17 September 2013. 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.

8 FINANCIAL PLANNING

8.1 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 requires a continued focus on cost control, an innovative approach to business transformation, robust change management processes and a sustained drive to improve efficiency. To ensure that the Council can continue to deliver its services within available resources the financial strategy continues to focus on the
delivery of a longer term financial plan. The Council agreed initial savings for consultation as part of the next 5 year financial plan to meet a range of pay, inflation, demographic and other service pressures on 12 December 2013. These are now included in the Administration’s five year revenue plan included for approval elsewhere on the Council agenda.

8.2 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 an estimate of cost of living increases of 1% in 2014/15 rising to a projected 2% for the remaining 4 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. Work has been ongoing through out the year to reach agreement with the Unions to change terms and conditions to better reflect how the Council delivers services and realise recurring proposed savings of £3.6m. In addition to assist with this strategy, the financial plan provides £2.9m over the 5 year period to fund early retirement/voluntary severance.

8.3 As part of the financial planning process assumptions are made about pressures and risk facing the Council over the next 5 years and whether a provision or level of provision is sufficient. The main areas that the Council continues to monitor are highlighted below.

8.4 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.

8.5 Welfare Reform

The Council is working with COSLA and the Scottish Government to address the impacts of Welfare Reform as they are identified and arise. While longer term proposals will be far reaching, the immediate effects on the Council’s Finances in 2014/15 are thought at this stage to be limited. The revenue budget provides for Council tax benefit and reducing housing benefits subsidy. The longer term implications of universal credit have yet to be addressed in the 5 year model.

8.6 Children’s Placements

The Integrated Children’s budget, with in the Social Work department, has seen an increase in demand for the number of looked after children requiring secure and residential placements during 2013. This has led to a budgetary pressure of £1.1m in 2013/14 which has been partially met by the department. If this level of demand for support continues into next year it will drive a strain on the budget of up to £1.4m. The demand for support to vulnerable children is difficult to predict and fluctuates throughout the year. To ensure that the financial strategy puts measures in place, to meet this potential change in demand, funding from a freeze in discretionary spend of £0.535m has been agreed by the Executive for
earmarking on the 21 January 2014. This service will continue to be monitored in 2014/15 and any continuing pressures will be reflected in the rolling 5 year financial plan.

8.7 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. The next valuation will take place in 2014 and the results of this exercise may impact upon the funding level and employers contributions. 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.

9 IMPLICATIONS

9.1 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.

9.2 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.

9.3 Equalities

There are no adverse equality implications arising from this report.

9.4 Acting Sustainably

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

9.5 Carbon Management

There are no effects on carbon emissions.

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

9.7 **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

10 **CONSULTATION**

10.1 The Corporate Management Team, Head of Corporate Governance, the Head of Strategic Policy, 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**

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<thead>
<tr>
<th>Name</th>
<th>Designation and Contact Number</th>
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<tbody>
<tr>
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<td>Financial Services Manager 01835 825018</td>
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</tbody>
</table>

**Background Papers:**

**Previous Minute Reference:** Council Report 12 December 2013 and Executive 21 January 2014

**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.

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