FINANCIAL STRATEGY 2015/16 – 2019/20

Report By Chief Financial Officer

SCOTTISH BORDERS COUNCIL

12 February 2015

1 PURPOSE AND SUMMARY

1.1 **This report seeks approval for the financial strategy for the Council covering the period 2015/16 – 2019/20.**

1.2 The Council, in common with other public sector organisations, continues to face significant and ongoing financial challenges as it aims to provide the best possible services within the resources available. In response to these challenges the Council has embarked upon a programme of transformation which aims to modernise services and restructure the organisation over the next 5 years. The corporate transformation programme will require the Council to make best use of its people, its resources, focus efforts to look after the Borders and improve efficiency and effectiveness.

In turn 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 priorities; and,

c) provides stability in resource planning and service delivery as expressed through revenue and capital budgets and approved Corporate plans.

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. The 5 year revenue financial plan has now been rolled forward to assess the likely level of resources available over that period and the budgetary adjustments that will be required to ensure spending plans remain affordable and the Council's finances remain sustainable in the longer term.

1.4 Firm figures have only been published via the Local Government Finance Settlement for 2015/16 and consequently it is recognised that beyond the next financial year the financial strategy can only be based on estimated resources. The 5 year plan is therefore based on the best information currently available and it will need to be adapted over time to respond to changing circumstances. The strategy uses an approach based on a quantified financial risk register to set the level of unallocated balances underpinning the 5 year plan.

2 RECOMMENDATIONS

2.1 It is recommended that Council approves the financial strategy for 2015/16 – 2019/20 as set out below:

- **a freeze on council tax in each year of the budget has been reflected pending a longer term national review of Local Government funding through the Council Tax Commission which may result in changes to Local Government finance during the 5 year period;**
- **set a prudent, sustainable budget in line with available resources;**
- **continue to invest in infrastructure through a sustainable capital programme financed by £20.71m loans charges in 2015/16;**
- **maximise income while keeping fees charged to service users at an affordable level;**
- **continue to invest in corporate transformation and efficiency projects to deliver long term financial savings and service benefits;**
- **focus on preventative revenue and capital spend; and,**
- **maintain unallocated reserves of £6.756m for 2015/16 in line with the assessed risk register in appendix 1.**

<u>Financial Strategy 2015/16 - 2019/20</u>

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 requiring 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 possible stimulus to the wider economy,
- protects the environment of the Borders
- protects those who are most vulnerable in society,
- seeks to focus spend on prevention designed to reduce future demand for council services by stopping problems arising or by addressing problems early on
- maximises the contribution from local collaboration arrangements
- recognises the need to continue to maximise efficiency and 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:-

- **a freeze on council tax in each year of the budget has been reflected pending a longer term national review of Local Government funding through the Council Tax Commission which may result in changes to Local Government finance during the 5 year period;**
- **set a prudent, sustainable budget in line with available resources;**
- **continue to invest in infrastructure through a sustainable capital programme financed by £20.71m loans charges in 2015/16;**
- **maximise income while keeping fees charged to service users at an affordable level;**
- **continue to invest in corporate transformation and efficiency projects to deliver long term financial savings and service benefits;**
- **focus on preventative revenue and capital spend; and,**
- **maintain unallocated reserves of £6.756m for 2015/16 in line with the assessed risk register in appendix 1.**

4 **FUNDING**

4.1 **Aggregate External Finance**
It is assumed the full level of AEF, estimated at £203.321m, excluding specific grants, will be deployed in setting the 2015/16 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 pending a longer term national review of Local Government funding through the Council Tax Commission which may result in changes to Local Government finance during the 5 year period. A band D equivalent of £1,084 for each of the next five years has been set with all other council tax bands varying as a set proportion of the band D figure. The Scottish Borders council tax product, following a review of properties, collection rates and levels of bad debt provision, is estimated as £51.602m in 2015/16 and £51.992m in 2016/17. 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 previously committed to providing support to an Affordable Housing Investment programme of £18.8m and to ring fence funding of £3.3m from 2nd homes council tax to offset land acquisition costs over the programme delivery period. The Government issued new guidance on the changes to 2nd Homes Council tax regulations in May 2013 to allow 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 2015.

Table 1 Funds and Balances	1 April 2015
	(Estimated)
	£'000
Statutory Funds	
Corporate Property Repairs and Renewals Fund	0
Plant and Vehicles Renewals Fund	2,550
Insurance Fund	1,238
Capital Fund Excl Developer Contributions	1,941
General Fund – Earmarked	
Devolved School Management	0
Specific Departmental Reserves	2,103
Allocated reserves	2,700
General Fund – Non-Earmarked	6,756
Total	17,288

5.2 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 adequate 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.

5.3 A Corporate Financial Risk Register (an updated version of which is attached at Appendix 1) has again been used as the basis for setting reserve levels in 2015/16 and future years. This approach seeks to quantify the risks facing the council's finances, including over optimistic saving assumptions, unplanned employment and pension cost increases, 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 directly informed by an assessment of the risks facing the Council. This approach 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 £6.756m in 2015/16. The unallocated balance projected at the 31st March 2015 is sufficient to cover 66% of the risks identified in the risk register should they materialise and reflects 2.65% of the 2015/16 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 2013/14 these adjustments were broadly neutral and therefore 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 2014/15 figures included £3.032m of balances earmarked for use in 2015/16 and the current year projected balances will increase if budgets are earmarked to future years during the course of 2014/15.

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

The 5 year revenue plan assumes the drawdown of £0.508m in 2015/16, £0.962m in 2016/17 and £0.153m in 2017/18 from reserves. 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.

5.8 **Recommended level of unallocated reserves**

A number of issues which have a bearing on the level of unallocated balances have been identified in the financial risk register set out in Appendix 1. These risks determine that the recommended level of unallocated reserves should be held at £6.756m.

6 TREASURY AND CAPITAL

6.1 **Treasury Management Strategy 2015/16**

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 plans, 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.

6.2 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 £20.71m for the first two years dropping to £19.91m in the last three years. This reduction in loans charges is a result of the planned repayment of specific consents to borrow for ER/VS and Icelandic Banks previously granted by Scottish Government.

6.3 Treasury Management earmarked balance

Council on the 25 September 2014 agreed to establish a Treasury management Earmarked balance within the General fund for the purposes of managing the costs of Treasury and financing activities within the council. The rationale for the establishment of this reserve was agreed with regard to anticipated future changes to the prevailing low interest rate environment. Council agreed therefore the establishment of the treasury reserve as an appropriate tactical mechanism to manage future treasury financing risk. The reserve provides the opportunity to smooth the impact of increasing costs of future interest rate rises on the Council's revenue budget over the medium term.

6.4 On-going Monitoring Of Capital Investment and associated costs

These 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.

7 FINANCIAL PLANNING

7.1 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 require 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 18 December 2014. These are now included in the Administration's five year revenue plan included for approval elsewhere on the Council agenda.

7.2 Staffing

Pay Awards Provision

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 2015/16 rising to a projected 1.5% 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. The agreement with the Unions to change terms and conditions to better reflect how the Council delivers services introduced over 3 years from April 2014 is on track to realise recurring savings of £3.6m. In addition to assist with this strategy, the financial plan provides £2.2m over the 5 year period to fund further early retiral/voluntary severance costs associated with the transformation agenda.

7.3 National Insurance

Looking further ahead, the 5 year revenue plan recognise the stated intention of the UK government to remove the current national insurance rebate which is received by the council as a provider of an occupational pension scheme contracted out of the second state pension scheme. This change it is estimated will cost the Council £2.7m per annum from 2016/17 unless further changes are made to national insurance rates and bandings to compensate. At present the financial plan assumes this cost will fall to the Council with no additional funding provided.

7.4 Local Government Pension Fund

The initial results of the 2014 triennial revaluation of the pension fund by the Council's actuary Barnett Waddingham have now been received. These show an improved funding position when compared to the last valuation undertaken in 2011. Overall the Actuaries initial assessment is that the previous deficit has been removed. Members will recall that at the 2011 valuation the Pension fund was 95.7% funded and a deficit recovery plan was put in place which assumed it would take 12 years to address the deficit position. The strong performance of the Pension fund over the last three years has allowed this deficit to be addressed over the much shorter 3 year period and consequently the funding level is now 100%. The rate of employer contribution for the Borders pension fund will remain at the current 18% over the 5 year plan. The long term view is that the fund remains in a healthy state with membership increasing. It should be noted that the Council's employer contributions are relatively low compared to the majority of Scottish Local Authority Pension funds and there may be a requirement for these contributions to increase in response to fluctuations in future investment returns, legislative change and as the membership structure of the fund evolves over time.

7.5 Teachers Pension Scheme

The Scottish Public Pensions Agency (SPPA) has been carrying out a review of the level of contribution for the Teachers' pension to determine the new employer contribution rate and employer cost cap which will apply from 1 April 2015. From 1 September 2015, employer contributions to the Teachers' pension scheme in Scotland will be payable at 17.2% of pensionable pay. This is an increase of 2.3% of pensionable pay compared to the current rate of 14.9% which has been paid since 1 April 2009. This increase has an annual cost impact of £1.1m in a full year. This pressure is due to the UK Government changing the discount rate used to value the schemes liabilities for 'unfunded' public sector pensions. This required the revised employer contributions to pick up the full cost of past and future pension costs. The Scottish Government recognises that an increase of this level is very challenging for scheme employers. The UK Government's approach to public service pension scheme reform means that the Scottish Government will not receive any additional funding to offset these costs and this additional cost has been built into the 5 year financial plan from 1 September 2015 with an assumption that the cost will be met by Council as a scheme employer. Discussions with Scottish Government over the funding of this pressure are continuing via COSLA.

7.6 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.

7.7 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 2015/16 and this will be kept under review over the five year period.

7.8 Early years

The revenue budget contains additional funding of £1.004m per annum providing total revenue funding of £2.196m to implement the Early Learning and Childcare provision as set out within the Children & Young People (Scotland) Act 2014, with 600 hours of Early Learning and Childcare being delivered for all 3 and 4 year olds and eligible 2 year olds. Four early years centres located within primary schools are being established with the first, located at Langlee being opened on the 6th November 2014. Places are available for all children in line with the entitlement in the Children & Young People (Scotland) Act 2014. Three year old children will be now able to access their place in the month after their third birthday. From August 2015, 2 year old children in families currently entitled to free school meals will also be eligible for 600 hours of early learning and childcare.

7.9 Children's Placements

Scottish Borders has seen a significant rise in the numbers of out of Area Placements and particularly those with Children with Social, Emotional and behavioural difficulties in recent years. A balance of £0.65m has previously been earmarked by the Executive to offset these costs and the revenue plan for 2015/16 assumes the drawdown of this balance over two years to be invested in staff working in an Outreach team to prevent young people being excluded from schools and being placed in out of area settings.

8 IMPLICATIONS

8.1 **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.

8.2 **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.

(c) The budget has been developed against the backdrop of ongoing negotiations regarding the freeze in teacher numbers between COSLA and the Scottish Government. Discussions with Government have indicated that an additional £8m will be made available nationally beyond figures announced in the December settlement letter. In return there is an expectation that teacher numbers will be maintained at 2014 levels and the Council's financial plan in 2015/16 is based on this target being delivered. Estimated additional resources of £0.17m have been reflected in year 1 of the financial plan based on 2.2% of teacher GAE.

(d) There is a risk that a draw down of general fund reserves will be required during 2014/15 as a result of adverse weather. Members will recall that £0.650m of the general fund reserves have previously been allocated to winter as part of the final revenue outturn for 2013/14. Currently the monitoring projects that expenditure in 2014/15 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 2015/16.

8.3 **Equalities**

There are no adverse equality implications arising from this report.

8.4 **Acting Sustainably**

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

8.5 **Carbon Management**

There are no effects on carbon emissions.

8.6 **Rural Proofing**

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

8.7 **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.

9 CONSULTATION

9.1 The Monitoring and Reporting Officer, the Chief Legal Officer, the Service Director Strategy and Policy, the Chief Officer Audit and Risk, the Chief Officer HR and the Clerk to the Council have been consulted and their comments have been incorporated into the report.

Approved by

David Robertson
Chief Financial Officer

Author

Name	Designation and Contact Number
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Background Papers:
Previous Minute Reference: Council Report 18 December 2014 and Executive 11 November 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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