

REPORT TO: THE MORAY COUNCIL ON 14TH MAY 2008

SUBJECT: FINANCIAL PLAN 2008 TO 2012

BY: CHIEF FINANCIAL OFFICER

1. REASON FOR REPORT

- 1.1 To agree a four year financial plan.
- 1.2 This Report is submitted to Committee in terms of Section A (1) of the Council's Administrative Scheme relating to the financial and budgetary policy of the Council.

2. RECOMMENDATION

2.1 It is recommended that Members:

- (a) consider the contents of this report;**
- (b) approve the four year financial plan detailed in the report;**
- (c) agree to target further efficiency savings of at least £3M to be implemented by March 2011 and assess the achievability of this target in light of the report from phase 1 of Designing Better Services, due to be reported in September 2008.**
- (d) note that the revenue budget and capital plan will be reviewed annually;**
- (e) note that all capital project allocations are subject to detailed reports being provided to the appropriate service committee.**

3. EXECUTIVE SUMMARY

- 3.1 This report deals with the allocation of £1 billion of funding to provide and support the provision of services to the population of the Moray area over the next 4 years.
- 3.2 The report describes: the work that has been undertaken to prepare the 4 year plan, the assumptions underpinning the plan and the risks in relation to: those assumptions and external factors resulting in substantial uncertainty. The major areas of uncertainty for the 4 year period are:
- Funding for Flood Alleviation Schemes
 - Demand levels for services to the elderly; and
 - Inflationary pressures, (including the impact of construction inflation on the Schools PPP project and other capital projects).

- 3.3 The report advises Members to target efficiency savings of at least £3M and to consider how achievable this target is when Phase 1 of Designing Better Services is reported in September 2008. This savings target is in addition to the £3.6M of savings identified in the report of which around £1.5M arise from efficiency measures.

4. BACKGROUND

- 4.1 The Revenue Budget and Capital Plan for 2008/09 were approved by the Council on 14th February 2008. The Budget Report to that Council meeting provided a summary of the background information that had been provided to Members since June 2007 in relation to the preparation of a Four Year Financial Plan.
- 4.2 Since the meeting on 14th February, Members have been provided with details of the potential capital projects for consideration in the five year Capital Plan and the strategy for developing the plan. The Administration Group has also been provided with a range of reports relating to requests for further information during their detailed assessment of Council services between September 2007 and January 2008.
- 4.3 Paragraph 3.2 of the Report to Council on 14th February stated that the Report was “a key milestone in establishing a policy led financial plan for the Council” and that the Administration Group “was at an advanced stage in completing the review work necessary to prepare a Four Year Financial Plan”. This Report provides Members with the Four Year Financial Plan proposals from the Administration Group.

5. REVENUE BUDGET - EXPENDITURE

- 5.1 The Four Year Revenue Budget is summarised on **APPENDIX 1**. The notes below provide a commentary on **APPENDIX 1**.
- 5.2 Departmental budget allocations have been made following the detailed review by the Administration Group as described in the Budget Report to the Council on 14th February 2008. There are a number of significant movements in budget allocations. The financial implications of the local priorities, published in late Autumn 2007, are set out on **APPENDIX 2**.
- 5.3 Provision for inflation and other cost increases is included in the allocations to services. The allocations are notional at this stage and the general inflation provision of 2.5% may require to be reviewed if current economic trends continue.
- 5.4 The Administration Group has considered a number of service issues in more detail and now recognises the need for additional budget allocations as follows:

	2008/09 £000	2009/10 onwards £000	
Building Repairs and Maintenance	400	590	APPENDIX 3.1
Autism	40	59	APPENDIX 3.2
Mental Health Services	44	156 *	APPENDIX 3.3
Museums Accreditation	15	22	APPENDIX 3.4
Area Committees	<u>50</u>	<u>200</u>	APPENDIX 3.5
	549	1,027	
	===	====	

Further details are provided in **APPENDICES 3.1 to 3.5** as referred in the table above.

* increasing to £324,000 from 2010/11.

- 5.5 The Concordat between the Scottish Government and COSLA sets out a package of measures that underpins the grant funding to Local Government in Scotland over the next three years. These measures include commitments in a number of specific service areas. Information provided by COSLA indicates that the notional allocations included in the finance settlement for these national commitments are £0.9 million in 2009/10 and £1.9 million in 2010/11. The Council is not in a position to prepare reliable estimates for the cost implications for all of the national commitments and the position is summarised on **APPENDIX 4**. Service Departments will provide detailed reports to the Administration Group, in the first instance, for further consideration as and when more information is available in these areas.
- 5.6 Regarding reducing class sizes it is notable that Devolved School Management Budgets have reduced by around £1.2M over the last 2 years due to the reduction in pupil numbers. Future roll reductions will clearly be relevant in relation to the financial impact of reducing class sizes. It should also be noted that the locations of where roll reductions take place is important. We have experience of years when the overall pupil roll has reduced but the budget is required to increase due to the distribution of the changes across Moray schools.
- 5.7 Loan charges are based on existing debt for previous capital projects and an estimate of the cost of new debt from the capital plan. The capital plan is dealt with in section 7 of this report.
- 5.8 The finance settlement from the Scottish Government includes funding towards the cost of operating the two new PPP schools. Information received from COSLA indicates that the funding included is: £195,000 for 2009/10 and £1.8 million for 2010/11. The Council is working to a timetable where the operating costs will be incurred from 2011/12 onwards with an annual contribution from the Government of £3.6 million. Meantime, the early inclusion of grant payment for the PPP scheme will give the Council some additional flexibility.

- 5.9 The Council approved savings of £2.3 million for 2008/09 on 14th February 2008. This included a target figure from the former ring fenced funded services of £276,000. The Administration Group has reviewed these budget allocations and the detailed proposals for 2008/09 allowing for the savings is attached as **APPENDIX 5** to this Report.
- 5.10 During the review of budget allocations, the Administration Group identified a number of additional savings and savings that could be increased beyond the amounts approved for 2008/09. The savings proposals that are additional to the approved savings of £2.3 million are summarised on **APPENDIX 6** to this Report.
- 5.11 The strategy for delivering the balancing savings target is set out in Section 9 of this Report. The remaining savings targets during the four year period are as follows:

	2008/09 £m	2009/10 £m	2010/11 £m	2011/12 £m
Savings Target	2.6	4.2	4.4	6.2
LESS: Savings Identified	<u>(2.3)</u>	<u>(2.9)</u>	<u>(3.3)</u>	<u>(3.6)</u>
Savings Targets	£0.3m =====	£1.3m =====	£1.1m =====	£2.6m =====

Therefore, based on the assumptions and estimates in this Report, the Council needs to identify and implement cost saving measures of £2.6 million by the end of March 2011. The position is complicated, in particular, by two key factors:

1. Reliability of Future Cost Estimates

The budget review process has identified that cost estimates may be understated in the following areas:

Care of the Elderly – the Head of Community Care has commenced work on projecting the likely demand levels for services for the next 4 years. Initial indications are that the increase in demand may well exceed the increase in the budget allocation for services to the elderly.

Inflationary Pressures – the budget assumption for inflation is based on 2.5% which is the current level of the Government's preferred measure of inflation, the Consumer Price Index. However, fuel and food prices are well in excess of this level and the Retail Price Index is currently at 3.8%.

National Priorities – the impact of reducing class sizes is uncertain. Further work is required in relation to most of the National Priorities.

2. Funding for Flood Alleviation Schemes

The updated expenditure profile for the Flood Alleviation Schemes is set out on **APPENDIX 8**. The finance settlement for the next three years results in a shortfall in grant requirement of £23 million and this is dealt with by the accelerated use of the Council's Capital Fund and additional borrowing. The peak of the additional borrowing is £13.4 million in 2010/11. However, if as described on **APPENDIX 8**, the grant level is increased to £80M in the following 3 year settlement, the shortfall will be addressed and this would result in cost reductions of around £0.6 million per year from 2013/14 onwards. This is the best position that the Council can hope for and the permutations below this figure are numerous. If Capital Grant levels for the current three years are used as a worst case scenario, then additional annual savings would be required to fund further additional borrowing of £41 million. Allowing for the use of £5 million from the Council's general reserves leaves £36 million which would require additional revenue savings of £2.3 million from 2011/12 to 2013/14.

In addition to the foregoing concerns it is now becoming apparent that construction industry inflation is impacting on the schemes resulting in the costs escalating.

6. REVENUE BUDGET - INCOME

- 6.1 The grant figures for 2008/09 to 2010/11 are the amounts advised to the Council by the Scottish Government in their Finance Circular 1/2008. The figure for 2011/12 assumes a 2.5% increase on the previous year. This increase is in line with prior year increases of around 3.5% of which 1% relates to additional expenditure on government priorities.
- 6.2 The additional grant in relation to the Council Tax freeze is one of the key components of the Concordat, referred to earlier. The figures for 2008/09 to 2010/11 come from Finance Circular 1/2008. The figure for 2011/12 assumes the same increase as in previous years. It should be noted that the percentage increase from this grant reduces each year as follows:

	2008/09 £000	2009/10 £000	2010/11 £000	2011/12 £000
Grant Increase as % of Council Tax				
Council Tax	36,222	36,494	36,767	37,043
Prior Year Grant Allocation	<u>-</u>	<u>1,142</u>	<u>2,283</u>	<u>3,425</u>
Notional Council Tax Base	36,222	37,636	39,050	40,468
Grant Increase for Council Tax Freeze	1,142	1,141	1,142	1,142
Grant Increase as a % of Notional Council Tax Base	3.2% =====	3.0% =====	2.9% =====	2.8% =====

- 6.3 Interest on the Capital Fund will cease to be available once that Fund has been fully utilised.
- 6.4 It is assumed that Band D Council Tax will remain at £1,135 for the four year period. This results in an average Council Tax rate for Moray households of £1,008 which compares with the rest of mainland Scotland as follows:

Average Council Tax	
Highest	£1,340
Average	£1,100
Moray	£1,008
Lowest	£943

The growth in volume of households liable for Council Tax has been estimated as 0.75% each year based on previous trends. This assumption will need to be reviewed annually.

The collection rate estimated for budget purposes is 98.7%.

7. CAPITAL

7.1 The Capital Plan is funded from three sources as follows:

- Borrowing
- Capital Grants; and
- Capital Receipts (from asset disposals)

The Council is required to adhere to the Prudential Code when considering how much to borrow to fund the Capital Plan. The key factors in the Prudential Code are:

- Affordability; and
- Sustainability.

Affordability

Capital Expenditure is one component of the Council's annual expenditure and affordability must therefore be viewed in that overall context. The draft Plan is affordable assuming revenue expenditure is maintained within the levels outlined in this Report.

The Prudential Code indicates that in setting the Capital Plan, direct reference be made to the implications arising from Capital Expenditure to Council Tax. An increase or decrease of £1million in Capital Expenditure for a single year would result in an increase or decrease in loan charges of £70,000. This is equivalent to a Council Tax increase of 0.2%. With the freeze on Council Tax likely be agreed for 3 years it is now more relevant to consider the impact on revenue expenditure resulting from any increase in loan repayments due to higher capital expenditure.

Sustainability

Sustainability needs to be considered in terms of (i) whether the Council can continue to afford the levels of investment proposed and (ii) whether current levels of investment will result in assets being maintained and/or replaced within acceptable timescales.

The draft plan identifies additional borrowing requirements as follows:

	2008/09	2009/10	2010/11	2011/12
	£M	£M	£M	£M
Core Capital Plan	10.0	12.7	16.2	12.6
Flood Alleviation Schemes	5.4	-	13.4	3.5*
Total Borrowing	<u>£15.4M</u>	<u>£12.7M</u>	<u>£29.6M</u>	<u>£16.1M</u>
	=====	=====	=====	=====

*Assumes significant additional capital grant for flood schemes in future years to bring the overall funding level from the government back to 80%.

Allowing for the repayment profile on the Council's existing debt of around £120M the net impact on loan charges each year will be:

	2008/09	2009/10	2010/11	2011/12
Increase in Loan Charges	£0.7M	£0.9M	£1.3M	£1.5M
	=====	=====	=====	=====

It should be noted that the increase in loan charges also varies due to the repayment profile of existing loans and the assumption that capital expenditure is incurred on average half way through each year.

The uncertainty regarding the loan charges from 2011/12 to 2013/14 due to the grant funding for flood alleviation schemes presents a significant problem for the Council. At this stage the first 3 years are affordable on the assumption that an efficiency savings programme can be established to balance the overall shortfall identified in this report. Years 4, 5 and 6 will need to be reviewed again when the finance settlement for 2011/12 to 2013/14 is announced by the Scottish Government.

- 7.2 The Council's Capital Plan is underpinned by the Asset Management planning arrangements in place in the Council. Whilst these arrangements are not yet fully developed, they do still provide a reasonable basis from which to assess the operational requirements in terms of asset replacement, development and major repair/refurbishment issues. Members were provided with detailed information on the capital investment requirements to maintain service levels and other bids for capital funding on 13th March 2008. The strategy document used to develop the draft Plan was also provided at that time. The Administration Group reviewed this information and the draft Plan attached as **APPENDIX 7** provides the outcome of that review. The amount of funding available for capital funding is heavily influenced by the Flood Alleviation Schemes and the expenditure plans for these schemes are detailed on **APPENDIX 8**. It should be noted that at the time of writing the estimates for the Rothes Scheme were being reviewed and it is understood that the costs for that scheme are likely to increase in the order of £3 million. This increase is due, primarily, to construction industry inflation and therefore the estimated costs for the other schemes are also likely to increase.
- 7.3 In addition to Flood Alleviation Schemes and the capital investment to maintain current service levels, the Administration Group has identified a number of priority areas that are included in **APPENDIX 7**. The main priority areas are:
- (a) School Estate
 - (b) Social, Emotional Behavioural Needs Bases
 - (c) Child Protection Unit
 - (d) Elgin Traffic Management
 - (e) Waste Management
 - (f) Industrial Estates
 - (g) Office Accommodation
- (a) School Estate

The School Estate Management Plan has been developed over a number of years and provides the condition and suitability information necessary to plan for improvements in the School Estate. The Administration Group have indicated that expenditure plans should be based on Suitability Level A and Condition Level B based on the definitions previously provided to Councillors. The Capital Plan includes £16.5 million over the five year period for investment in the School Estate plus a further £3 million for Elgin High School and associated sports facilities. Further reports will be provided to Educational and Social Services Committee on the detailed expenditure proposals for approval.

(b) Social, Emotional and Behavioural Needs Bases

During the next three years, £1 million is included in the Plan to enable these bases to be established at all secondary schools in Moray. The Administration Group recognise the importance of these facilities in addressing the ever increasing number of children requiring additional support, often resulting in costly out of area placements.

(c) Child Protection Unit

The requirement for this unit has been reported to and approved by Council Members.

(d) Elgin Traffic Management

The plan includes £10M to deal with Elgin Traffic Management. Based on previous reports to the Council, this amount will be insufficient to deliver all of the infrastructure projects identified in the Development Plan. Further consideration will need to be given to establish affordable proposals for implementation during the five year period.

(e) Waste Management

There is also just over £10M in the plan in relation to additional waste management facilities to enable the Council to continue to reduce the volume at waste disposal at the landfill site. The methods to be used to achieve this have yet to be fully assessed. The next stage is to undertake a detailed study and report back to the Council on the investment requirements to assist in the strategy for the continuing reduction in waste to landfill.

(f) Industrial Estates

The Administration Group identified that further investment is required to provide business premises to meet the demand for such premises and ensure that economic development is supported appropriately by the Council. In addition to the budget to refurbish existing premises a further £2M has been allocated to provide new sites and premises. Detailed proposals will be provided to the service committee responsible for economic development in due course.

(g) Office Accommodation

The Council identified the need to rationalise and modernise office accommodation a number of years ago and has received many reports in relation to the options that have become available. The Asset Management Working Group has identified that there are currently 4 potential options and aim to provide an initial report to compare these options and consider the feasibility of the best of the 4 options against

continuing to operate from the multitude of small office facilities, many of which are not fit for purpose and do not provide a good basis for service modernisation.

- 7.4 All Capital Plan allocations are subject to detailed Reports being provided to and approved by the relevant Service Committees. These Reports must include full details of:
- The work to be undertaken
 - The benefits associated with the project
 - A reliable estimate of costs

If the project has any ongoing additional revenue implications, these must also be identified and Committee must identify how these costs will be met before approving any project.

- 7.5 Within the past few months Members have been advised of the impact of construction industry inflation on the Reiket Lane bridge and in para 7.2 the same issues was highlighted in relation to the flood alleviation schemes. These have also been reported in the press recently about alleged cartels in the construction industry. This environment makes it very difficult for reliable estimates to be prepared for large capital projects and will reduce the amount of work that can be delivered from the limited capital resources available.

8. **RESERVES**

8.1 General Reserve

	£M
Balance at 1 st April 2007	10.9
Less: Commitments	(2.2)
Estimated Outturn 2007/08	0.4
ESTIMATED BALANCE AT 31ST MARCH 2008	<u>£9.1M</u> =====

The Council has agreed that £1M of the above fund is to be made available for spend to save projects.

Reference is made to the issues identified in the early sections of this report and in particular the uncertainty regarding funding for the Flood Alleviation Schemes. One item that has not been mentioned elsewhere in the report is the potential liability for remaining equal pay claims. In the most recent update report to Policy Committee Members were advised that the potential liability if all claims lodged are successful, is estimated at £1.6M. Meantime Members are advised to take a cautious approach to the use of existing reserves.

8.2 Capital Fund – it is anticipated that this fund will be fully utilised during 2008/09.

8.3 Other Reserves

Coastal Protection Fund	£57,000
Printing – Equipment Replacement	£64,000
Flood Repair Fund (Insurance excess re: Flooding)	£2,080,000
Insurance Fund (Insurance excess re: school fires)	£1,227,000

9. EFFICIENCY SAVINGS

9.1 The purpose of a medium term financial plan is to allocate resources in accordance with Council priorities and provide budget managers with a reasonable degree of certainty to support service planning. Experience shows that during the period of a 4 year plan there will be changes in many factors including demand that will result in variances from budget and the need to review and amend budgets. This can be seen most recently in the budget monitoring report to Policy Committee on 30th April 2008 which identifies underspends of £2.4M and overspends of £2.0M giving a net underspend for the year of £0.4M. This background provides the context against which to consider the timetable for delivering efficiency savings.

9.2 As indicated in para 5.11 the remaining savings targets are:

	2008/09	2009/10	2010/11	2011/12
Savings Targets	£0.3M	£1.3M	£1.1M	£2.6M
	=====	=====	=====	=====

The targets are cumulative, therefore if annual savings of £0.3M are implemented in 2008/09 the target for 2011/12 will be reduced by this amount to £2.3M.

9.3 The Administration Group have continued to look at further savings opportunities and since the annual budget was set they have started to look at the wide range of services provided to Young People (loosely defined as those in the age range 16-24). A target saving of £0.5M has been set by the Administration Group for this area of service provision.

9.4 The savings target for year 4 of £2.6M, is based on the many assumptions in this report. A realistic view of the risks associated with:

- Flood Alleviation Scheme Funding
- PPP Schemes Affordability Gap
- Inflationary Pressures
- Care of the Elderly

would indicate that the savings target of £2.6M is unlikely to be sufficient and that a minimum of £3M would be a more responsible target.

- 9.5 The Council is taking part in the National Shared Services Diagnostic project to identify improvements and efficiencies in the delivery of council services. The Moray project is called Designing Better Services. The project is progressing well and in September a report will be provided to Members detailing the main opportunities for improvement and efficiencies identified during the review. That report should provide the Council with an indication of the potential for change and the potential for efficiency savings arising from their implementation.
- 9.6 It will be clear from the foregoing paragraphs that managing the financial position over the next few years will require continuing close monitoring and review. As far as further savings are concerned, at this time, the Council is advised to focus on the longer term position and target efficiency savings of at least £3M to be implemented by March 2011. The target figure should be reviewed again after the Council has received the report from Phase 1 of the Designing Better Services project in September.

10. POLICY LED BUDGETING

- 10.1 In a report to the Policy Committee on 29th August 2007 a description was provided of how the Council's financial planning arrangements are integrated with the overall Council planning framework. The report indicated that budget allocations needed to reflect:
- Demographic changes and the impact on demand
 - Council Priorities
 - Community Planning Priorities; and
 - National Priorities

For these issues to be fully reflected in the budgets for the Council's 80 Activities requires budget decisions to move resources to match to the priorities identified. The pursuit of further efficiency savings will also be key to enabling the delivery of these priorities.

- 10.2 The link to Community Plans and Corporate Plans has been dealt with in various ways in the past and it is important to recognise the importance of the Single Outcome Agreement in the context of Council and Community Plans and therefore the financial plan. This is a new approach that is integral to the Concordat between COSLA and the Government and is likely to provide an opportunity to reassess the need for existing planning documents. Delivery of the outcomes in the Single Outcome Agreement will be dependant on resources being directed in accordance with that agreement and this will need to be reflected formally in future planning processes.
- 10.3 A great deal of what the Council provides is governed by legislation and the opportunity for shifting resources is therefore limited. Resistance to change is also a significant issue that requires careful consideration and judgement by Members – the reality is that the start of a new budget period does not present a blank sheet for planning purposes.

10.4 Against the background described above the financial plan for 2008/09 to 2011/12 provides evidence of a policy led approach in the following areas:

- (a) Process – Members are involved in a very detailed examination of council services and budget allocations. This process ensures that risk, performance impact and relative priorities can all be considered.
- (b) Funding for Priority Areas
 - Local priorities as identified on **APPENDIX 2** and within the Capital Plan.
 - National priorities as identified on **APPENDIX 4**.
- (c) Balancing the Budget
 - substantial growth in the priority areas referred to above will be funded by efficiency savings and reductions in lower priority areas.

11. **LONGER TERM PLANNING**

11.1 The Council is encouraged to consider issues affecting the Moray area beyond the 4 year financial plan horizon, with longer term planning covering 10 or more years depending on the service area concerned.

11.2 The Council is engaged in longer term planning in a number of areas as follows:

- Asset Management Planning – including the School Estate Management Plan, Roads Infrastructure and Office Accommodation.
- Housing Revenue Account – 30 Year Development Plan
- Moray 2020 – Economic Development

11.3 The Council recognises the need to collate information in the following areas to enable consideration of impacts on services.

- Demographic Changes – Growing elderly population and reducing population of children.
- Asset Management – Develop information capture and reporting.

Further work will be undertaken in these areas to support future medium term and longer term plans.

12. SUMMARY OF IMPLICATIONS

(a) Corporate Development Plan/Community Plan/Service Improvement Plan

See Section 10.

(b) Policy and Legal

See Section 10.

(c) Resources (Financial, Risks, Staffing and Property)

Dealt with throughout the report.

(d) Consultations

The Corporate Management Team have worked with the Administration Group on the development of the 4 year financial plan.

Staff Unions have been advised of the process for developing the 4 year financial plan and have been briefed on the overall implications. They have also been advised that any changes impacting on staff will be subject to consultation in the usual way.

13. CONCLUSION

13.1 See Executive Summary at Section 3.

Author of Report: Mark Palmer, Chief Financial Officer

Background Papers:

Ref: MP/LJC/431453/433526/433932/433945/433553/433600/
433610/433616/433624/424300/433638/433981/434149/
434147