

REPORT TO: East Lothian Council

MEETING DATE: 25 October 2016

BY: Depute Chief Executive (Resources & People Services)

SUBJECT: Financial Prospects 2017–2020

1 PURPOSE

- 1.1 To provide an overview of the Financial Prospects for 2017/18 and beyond to help inform the development of the 2017–20 budget, and to set out the process to be followed for the public budget consultation.

2 RECOMMENDATIONS

- 2.1 Members are recommended to note:
- the financial prospects for 2017/18 and beyond for the Council
 - the potential implications arising from the Scottish Government's proposed Council Tax Reforms and the need to promote greater public awareness
 - the process for the 2017–2020 budget development
 - that the public budget consultation will be launched shortly

3 BACKGROUND

Financial Strategy

- 3.1 The existing Financial Strategy covering the period 2016 through to 2019 was approved by Council on 9 February 2016. This strategy places a continued focus upon:
- **Delivering an enhanced Change Programme** that will support the achievement of significant efficiency savings across all service areas and all resource inputs such as staffing and supplies;
 - **Constraining cost growth** – through effective demand management, good financial control by managers and by effective procurement and contract management with suppliers;

- **Generating additional income** and ensuring that, where the Council has decided to charge for services, there is maximum cost recovery;
- **Progressing partnership working** where there are proven efficiency and or service gains;
- Continuing to **manage the General Services Loans Fund** ensuring affordability across the three years of the Strategy.

3.2 The audited 2015/16 year-end financial position was recently reported to and approved by Council on 23 August 2016, with the Council delivering a surplus and therefore an increase to reserves of £5.748m. The report confirmed my opinion that the current financial strategy remains on track to remove the future dependency upon reserves; however, it also confirmed that many significant financial challenges still lie ahead of us. It is anticipated that the prolonged period of financial austerity measures across the public sector will largely continue, and also that we face major challenges in satisfying the additional infrastructure requirements associated with both the proposed new Local Development Plan, and any proposed City Deal for Edinburgh and South East Scotland. Developing future sustainable operating budgets within a reduced cost base remains a critical balancing component in order to meet new cost and demand pressures emerging across a wide range of service areas.

3.3 Cabinet has also recently considered a report on the financial position at the end of the first quarter in 2016/17. Despite a positive in year financial position, I classified two service areas as being 'High Risk' with a further two as 'Medium Risk' signalling that within these service areas there is a significant risk that services will not be delivered within approved budgets. The 2016/17 financial performance will continue to be closely monitored by officers, with a more detailed review of the Q2 position and assessment of the 2016/17 projected outturn being considered as part of developing future years' budgets.

Financial Outlook

3.4 A key component in setting any Council budget is the funding received through the grant settlement from the Scottish Government. When setting the existing 3-year budget for 2016–19, only one year grant figures had been published by the Scottish Government and therefore our planning assumption that the Council will receive a 'flat cash' grant settlement figure was reflected through until 2018/19, in other words – no additional grant has been forecast in each of the next two years.

3.5 It is now known that the UK Government's Autumn Statement will be published on 23 November 2016, with most recent confirmation that both the Scottish Government Budget and Local Government Finance Settlement will be published on 15 December. Although similar to last year, more typically this is later than normal and will place considerable pressure upon the Council's own budget development process. The impact of the UK's decision to exit the European Union will most likely be a central part of the new Chancellor's financial strategy, and there

remains considerable uncertainty as to what this may mean for the funding received by the Scottish Government, and in turn the funding settlement for Scottish Local Government and in particular for East Lothian Council.

- 3.6 Notwithstanding this unprecedented level of uncertainty, a number of independent financial commentators continue to signal the potential for future funding reductions (especially revenue) at both a UK and Scottish level and as such there is a high risk that the current grant planning assumption of 'flat cash' is optimistic. In addition to the wider UK/Scottish Government funding variables surrounding the grant settlement, there are a number of others that will impact upon the overall level of resources which we receive locally through grant support. These include areas such as any new policy initiatives, changes to existing policy, or indeed changes to grant distribution indicators, all of which can have either a positive or negative impact on the final grant settlement.
- 3.7 As indicated above, the further refinement of government grant planning assumptions will be a key feature of the budget discussions over the coming months and will clearly have a major influence on the extent of any potential budget gap. A further challenge may arise from a recent trend that has seen an increased level of ring-fencing whereby the settlement has come with an increased number of specific conditions and associated sanctions, which in turn limits the financial flexibility which local authorities can apply to help satisfy local pressures and priorities. COSLA continue to lobby against the imposition of such specific conditions but it is uncertain to what extent, if any this will be successful and therefore this will need to be considered as part of any forward budget planning.

Scottish Government Council Tax Reform Proposals

- 3.8 From April 2017, one substantive variable which if introduced, may impact upon the level of funding received by this Council through the Local Government Finance Settlement, is the proposed change to the Council Tax Multiplier. A joint Scottish Government and COSLA review of Local Taxation was published in December 2015, with no definitive recommendation on the most appropriate form of local taxation, but a clear recommendation that the current Council Tax system should not continue in its current form. In March 2016, the Scottish Government published its proposals for reform of Council Tax the implications of which are set out below.
- An increase in the ratios of the upper bands (E–H) relative to Band D, which will mean that the bills in these bands (based upon existing Band D equivalent for 2016/17) will increase by the following, with Bands A to D remaining unchanged:

Band	Current Rate of Council Tax (£)	Proposed Rate of Council Tax after Multiplier (£)	Impact of Multiplier (£)	Impact of Multiplier (%)
Band D	£1,118	£1,118	£0	0%
Band E	£1,366	£1,468	£102	7.5%
Band F	£1,614	£1,816	£202	12.5%
Band G	£1,863	£2,189	£326	17.5%
Band H	£2,235	£2,738	£503	22.5%

- As part of their formal Council Tax Reform Proposals, the Scottish Government has proposed that the additional revenue received by all councils as a result of the change in multipliers identified above will be used to provide an additional £100 million per annum to an expanded national Education Attainment Fund which will be distributed directly to schools. This proposal is directly aligned to the Scottish Government's recently published Education Delivery Plan, as part of raising School Attainment levels, something that the Council is taking forward through planned engagement activities with relevant stakeholders and will be considered separately by the Education Committee in November.
- After a period of nine continuous years, the Scottish Government has also proposed to end the current Council Tax freeze albeit with a new proposal to cap any increase in Council Tax proposed by an individual local authority at 3% per annum, coincidentally the same level as that contained within the existing 3-year budget. The impact of any such increase actually proposed by East Lothian Council for 2017/18 would be applied prior to the application of the additional multipliers above.

3.9 The proposed changes to Council Tax multipliers give rise to a number of areas that merit further consideration and some of these are set out below.

- Council Tax is widely regarded as one of the most visible forms of taxation. Despite this, and recent media coverage of progression of the reform proposals through the parliamentary process, there would appear to be relatively low levels of public awareness of the implications arising from the Scottish Government changes to the Council Tax multiplier and specifically that they will result in significantly increased Council Tax bills for all properties within Bands E–H. (In East Lothian this will impact upon more than a third of all households.) Most residents naturally associate any changes to local taxation with local policy decisions, and the true

nature of this change will need to be carefully communicated to the affected residents of East Lothian.

- This proposal raises fundamental questions of the long-established direct linkage between any money that is raised locally is also spent locally. It is important to stress that discussions about how the money raised through additional council tax and indeed how it is then allocated to schools are still on-going, with the Scottish Government currently indicating strong support that funding will be directed to schools, based upon the numbers of children in primary school and young people in S1 to S3 who meet existing eligibility criteria for free school meals (FSM). In practice this will mean a change to both; how the funding of schools is traditionally received, which is normally through the Revenue Support Grant; and secondly that for East Lothian, we will almost certainly raise significantly more money locally from the change in the council tax multiplier than is likely to be received in terms of direct funding for schools. Early indications would suggest that this could be less than 50% of the actual funding generated through additional Council Tax contributions.
- It has been suggested that for some people deemed to be on low incomes there will be exemption or relief but no specific details are yet available.
- There is also some uncertainty regarding whether or not the new bandings will also apply to any charges imposed by Scottish Water. Should any way forward require a charging mechanism that differentiates making use of two different banding sets would inevitably generate some confusion and would also require significant and urgent changes to our billing systems.
- Furthermore, the proposals change the traditional accountability framework for local public funds. The proposed direct allocation of money to schools means that local councils and their supporting governance arrangements are at risk of being by-passed.

Budget Development

3.10 Construction of budgets in any financial year is informed directly by the Council's 3-Year Financial Strategy that in turn is rooted to proper stewardship of taxpayer's funds. The budget development process for 2017/18 and beyond will be informed by the existing budgets for General Services (2016–19) and the HRA (2016–21), both approved by Council in February 2016. Typically, these budgets are rolled forward, and a rigorous validation process is then applied. This includes:

- Review of the 2016/17 financial position against the already planned 2017/18 budgets. This is critical to the baseline budget validation, with the Quarter 2 position and related projected outturn for the year being an important 'test' in respect of the financial sustainability of future budget plans.

- Validation that the all key planning assumptions reflected within the baseline budget remain accurate and appropriate. In addition to the assumptions on likely grant settlements discussed earlier in this report, this includes many contractual and inescapable commitments such as; pay and pensions, NDR and debt charges. This also includes a range of other areas including: Council Tax modelling and yield; related demographic assumptions including the service volume implications associated with changing school rolls and increased number of households; as well as our local commitments relating to either Scottish or UK Government policies such as Welfare Reform.
- Review the robustness and deliverability of existing planned efficiencies within 2017/18 and 2018/19.
- Review and identification of current and emerging financial pressures across all services. This will include any new or emerging legislative provisions such as the new Apprenticeship Levy and will also take into account significant pressures upon our council tax and rent collection now being experienced following the recent introduction of the Universal Credit Full Digital Service.
- The East Lothian Integration Joint Board became fully operational in April 2016. It will be necessary to recognise the role of the IJB in budget setting as well as the challenges and opportunities that will arise through closer alignment of both Health and Local Authority budgets.

3.11 Within the budget development process, a clear and early indication as to the baseline budget validation is critical to both assessment and understanding of any financial implications, and the Finance team are already working with CMT and services to secure early validation as quickly as possible.

Capital Planning

3.12 Proper budget validation applies not only to the General Services and HRA revenue budgets but also to their respective capital budgets, and the associated revenue implications in respect of debt charges. The Council's budgetary approach continues to look forward on a medium term basis of 3 years for General Services and 5 years for the HRA, however both are informed by a longer term capital planning view.

3.13 Due to the many and complex uncertainties that prevail, it is fair to say that anything beyond short term planning is currently very challenging and this is equally true in respect of any future Capital Grant support provided by Scottish Government, something that is again tied into the formal settlement.

3.14 More locally, however, there are also many variables that have the potential to impact significantly upon future capital budgets and these effectively challenge the Council such that the case for adopting a longer-term planning outlook is becoming much stronger.

- 3.15 The Council has recently approved a proposed Local Development Plan (LDP) which is currently out for statutory representation with any final plan unlikely to be formally adopted until beyond the more immediate 2017/18 budget considerations but within the existing 3-year budgetary planning period. It will be necessary to align our capital planning more directly with the LDP recognising the significant shift necessary to fund rising capital investment with greater prominence given to the capital income that can be secured through a revised developer contribution framework and the disposal of surplus assets. Such an approach would also enable us to better evidence need and therefore help secure additional external financing that would in turn, help unlock growth.
- 3.16 A further and potentially significant variable in respect of potential levels of future capital investment is the proposed Edinburgh and South East City Region Deal (ESECRD). In accordance with the policy direction already approved by Council, we continue to work within the ESECRD partnership in pursuit of a formal deal with both UK and Scottish Governments. Although these negotiations are still very much ongoing, discussions are going well and it is expected that some form of supporting statement will be made within the UK Chancellor's Autumn Statement and it is hoped that a formal deal might be announced in his March budget.
- 3.17 All of these elements will have implications both for the Council's General Services and HRA capital plans, and any associated revenue costs.

Next Steps

- 3.18 The coming weeks and months form a critical part of our budget development process. As mentioned earlier, the focus will remain on early validation of the baseline budget and refinement of existing planning assumptions, central to which is the level of government grant that the Council is likely to receive. This validated baseline budget will then form the platform upon which remaining service and financial challenges will be considered by the CMT and respective political groups.
- 3.19 In a similar way to recent years, the Council's budget decisions will also be informed by the public's views around local priorities. It is currently anticipated that the Council's public budget consultation in respect of both the General Services budget and the statutory HRA rent consultation will be launched during November. This will allow both council tax payers and rent payers to submit their respective views which will in turn be considered as part of the decision making process supporting the development of budget proposals.
- 3.20 A detailed budget development timetable has not yet been finalised although it is likely this will be built around the following key dates:
- Validation of existing 3-year budget underway
 - Public/Tenant Budget Consultations mid-Nov to Dec 2016

- UK Autumn Statement 23 Nov 2016
- Scottish Government Budget/Settlement 15 Dec 2016
- Draft Base Budgets to political groups before Festive Break
- Special Council Meeting 14 or 21 February 2017

4 POLICY IMPLICATIONS

- 4.1 There are no direct policy implications associated with this report although ongoing monitoring and reporting of the Council's financial performance is a key part of the approved Financial Strategy.

5 INTEGRATED IMPACT ASSESSMENT

- 5.1 The subject of this report has been considered and given there is no change in policy direction, there is no requirement to undertake any further impact assessment.

6 RESOURCE IMPLICATIONS

- 6.1 Financial – as described above
- 6.2 Personnel - none
- 6.3 Other – none

7 BACKGROUND PAPERS

- 7.1 Council 9 February 2016 – Item 1 – Council Financial Strategy 2015-18
- 7.2 Council 9 February 2016 – Item 5a – Budget Proposals – Administration
- 7.3 Council 23 August 2016 – Item 4 – 2015/16 Financial Review
- 7.4 Cabinet 13 September – Item 3 – Financial Review 2016/17 – Quarter 1

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