

# Finance and Resources Committee

10.00am, Friday, 14 February 2020

## Council Change Strategy 2020/23: Risks and Reserves

Executive/routine Wards Council Commitments	Executive All
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### 1. Recommendations

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- 1.1 Members of the Finance and Resources Committee are asked to:
  - 1.1.1 note the content of this report; and
  - 1.1.2 remit the report to The City of Edinburgh Council for approval on 20 February 2020 as part of the budget-setting process.

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## Council Change Strategy 2020/23: Risks and Reserves

### 2. Executive Summary

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- 2.1 The report advises members of the risks inherent in the revenue and capital budget framework and the range of measures and provisions established to mitigate these.
- 2.2 The report outlines the level of reserves held and the purpose for which they are maintained, including consideration of the adequacy of balances held to mitigate against known risks.

### 3. Background

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- 3.1 This report advises members of significant risks identified in the budget process and sets out the range of measures and provisions in place to mitigate these.
- 3.2 Unallocated reserves are held against the risk of unanticipated expenditure and/or reduced income arising in any particular year. In addition, there are specific earmarked reserves set aside to manage timing differences between the receipt of income and incurring related expenditure, in accordance with accounting rules.
- 3.3 The reserves held by the Council are reviewed annually as part of the revenue budget-setting process. The review considers the level of balances, the risks inherent in the budget process and the adequacy of arrangements in place to manage these known risks.

### 4. Main report

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#### Risks

- 4.1 Risks form an integral part of the budget process. What is important, however, is that these risks are identified, actively managed and, where appropriate, mitigated. Appendix 1 shows a matrix, setting out how it is planned that the known risks identified in this report will be managed. This list is, however, not exhaustive due to both the complexity and diversity of the changing environment within which the Council operates.

## **Future funding settlements**

- 4.2 Uncertainty around future funding settlements poses a significant risk to the Council's ability to set a balanced budget, given its impact on the overall level of savings required. While the provisional 2020/21 Local Government Financial Settlement (LGFS) was announced on 6 February, this only covered one year as opposed to the multi-year settlement originally envisaged. A more detailed commentary on the implications of the announcement is included in the Change Strategy report elsewhere on today's agenda.
- 4.3 Future years' funding allocations could also vary for a number of other reasons, including the use of updated population data and complexities of the funding distribution formulae, as well as wider Scottish and UK Government fiscal policy. In addition to the impact of methodological changes to be applied as part of the 2020/21 Settlement, in the medium-term a more fundamental Scotland-wide review of funding distribution has been initiated, with the potential for material changes in allocations to occur. The Council's actual funding allocations are additionally affected by the influence of the stability and 85% per capita funding floors, from each of which it currently benefits.

## **Delivery of approved savings and management of underlying service pressures**

- 4.4 Shortfalls in the delivery of approved savings and management of underlying service pressures are an on-going risk to the budget. In 2019/20, while 92% of service-specific savings are currently anticipated to be delivered by the year-end, the equivalent figure for Council-wide efficiencies is assessed at a much lower 62%. In light of these difficulties in delivery, subsequent years' efficiency targets within the budget framework have been considerably reduced.
- 4.5 Corresponding measures are also required to offset significant pressures within a number of demand-led areas of service, with many of the measures applied in 2019/20 being of a non-recurring nature. Given their magnitude, it is unlikely that structural pressures within services can be fully mitigated on a sustainable basis and the budget framework therefore incorporates a corresponding contingency of £10.4m in 2020/21, reducing slightly in subsequent years. This service investment can, however, only be afforded through the delivery of corresponding savings elsewhere within the budget. While consideration will be given to including an appropriate risk contingency within the framework to provide a safeguard against subsequent partial or non-delivery of some approved savings, there is a risk that this sum is insufficient to address any shortfall, particularly in the case of more complex or difficult savings measures.

## **Demographic changes leading to rising service demands**

- 4.6 Demographic changes continue to increase the overall level of demand for the Council's services and the ability to provide for this within available resources. Current levels of provision have been reviewed in light of updated population and pupil roll projections, resulting in the inclusion of total demographic-related

investment of £4.2m in the 2020/21 budget framework plus full pass-through of additional health and social care funding provided within the LGFS, with similar incremental increases assumed in subsequent years. More effective demand management, greater use of preventative approaches to service delivery and service prioritisation will, however, likely be required in order for this level of funding to prove sustainable.

### **Income**

- 4.7 Assumptions are made in the budget process on the level of income that can be generated by services. There are risks associated with these assumptions, primarily around (i) demand for and/or price sensitivity of chargeable services, (ii) timing of implementation of new or amended charges and (iii) the ability to collect all the income due. The Council has a range of measures in place to mitigate these risks, such as application of appropriate debt policies, service level agreements with external users and regular monitoring of income levels as a prompt to remedial action.

### **Legislative changes**

- 4.8 Legislative changes present on-going risks to the budget framework, and while provision has been made for the projected impact of known factors, such as superannuation increases for teaching and non-teaching staff, there is a risk that further changes are made, resulting in direct or indirect impacts on the Council's budget. It is additionally assumed that all of the savings measures set out in the Change Strategy report elsewhere on today's agenda are fully within the Council's gift. This remains to be confirmed in the case of both the proposed level of Council Tax rises and application of a savings target to the Integration Joint Board, each of which is based on the equivalent treatment in the 2019/20 Settlement.
- 4.9 The United Kingdom's exit from the European Union in January 2020 may result in economic uncertainty with a knock-on impact on the availability of staff in key service areas, increased demand for the Council's services and higher prices for some goods and services (particularly food), as well as wider levels of public expenditure. The Council has on-going risk assessment arrangements in place (including a Brexit-specific risk register), with contingency planning actively discussed at relevant working groups, and its level of preparedness was favourably assessed in the 2018/19 Annual Audit Report. Any specific financial implications will, however, be kept under review as the precise impacts become clearer.

### **Legal claims and inquiries**

- 4.10 There is a risk that the Council is exposed to reputational and financial consequences of legal claims and inquiries in relation uninsured and insured incidents. The on-going Scottish Child Abuse Inquiry has potentially significant financial implications but, at this stage, the precise impact on the Council (and any associated external funding) remains to be confirmed. There is a risk, nonetheless, that substantial additional funding to meet liabilities will require to be identified.

## **Major infrastructure projects**

- 4.11 The long-term financial implications of some major infrastructure projects, particularly the Local Development Plan, are still emerging. While the revenue and capital budget frameworks incorporate some provision in these areas based on current projections, there is a risk that the Council will require to support additional borrowing and/or revenue running costs associated with these projects. On-going review of the projects and potential timing and value of funding requirements will therefore continue to be undertaken through relevant project boards and risks escalated as appropriate.

## **Reserves**

- 4.12 Members are aware that the Council holds a number of earmarked reserves within the General Fund. As of 31 March 2019, the General Fund balance stood at £144.845m, of which £131.820m was earmarked for specific purposes. The unallocated General Fund balance remained at £13.025m, in line with the medium-term strategy of the Council.
- 4.13 There are significant planned applications of earmarked reserves during 2019/20 (some £37.3m), in line with the Council's wider financial strategy, with a projected balance of £107.564m at 31 March 2020. The plans include use of £18m from the Council Tax Discount Fund to support expansion of affordable housing provision within the city and drawdown from the Council Priorities Fund to manage in-year service pressures. Appendix 2 shows the planned use of these balances in the financial year 2020/21, insofar as they are known at this stage.
- 4.14 On 21 November 2019, the Council approved the allocation of £0.902m of available funds from the City Strategic Investment Fund (CSIF) to be transferred to the unallocated General Fund, increasing this fund from £13.025m to £14.072m as at 31 March 2020, inclusive of the in-year repayments due to the CSIF. Further increases linked to these repayments will increase the unallocated General Fund reserve by £0.145m annually.

## **5. Next Steps**

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- 5.1 Following Committee's consideration, the report will be referred to The City of Edinburgh Council for approval as part of the budget-setting process.

## **6. Financial impact**

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- 6.1 The report identifies where funding has been made available for the risks set out. The Council holds unallocated General Fund reserves against the likelihood of unfunded risks occurring.

## **7. Stakeholder/Community Impact**

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7.1 There are no direct impacts arising from this report.

## **8. Background reading/external references**

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8.1 [City Strategic Investment Fund](#) – City of Edinburgh Council, 21 November 2019.

## **9. Appendices**

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Appendix 1 – Risk Matrix

Appendix 2 – Projected Movement in General Fund

## Appendix 1

### Risk Matrix

The table below summarises how the risks identified in the report are managed.

<b>Risk</b>	<b>Provisions and other actions to manage</b>
Future funding settlements	<p>Provisions made in the Long-Term Financial Plan (LTFFP)</p> <p>Regular monitoring of public expenditure projections and active membership of relevant professional forums, promptly recognising potential or actual grant variations in LTFFP</p> <p>Development of longer-term Change Strategy to recognise the potential for variation from baseline assumptions in any given year and, by extension, an ability for additional savings measures to be accelerated</p>
Delivery of approved savings and management of underlying pressures	<p>Regular CLT and elected member scrutiny of proposed savings at the inception, development and delivery stages</p> <p>Regular SMT consideration of overall service budgetary position, including known or emerging risks and pressures, with a view to taking prompt corrective action</p> <p>Baseline level of additional investment included in 2020/21 budget framework, aligned to key areas of pressure</p> <p>Budget re-alignment, where required, to facilitate enhanced ownership, accountability and transparency of reporting</p>
Demographic changes leading to rising service demands	<p>Provisions made in LTFFP and regular reviews of the adequacy thereof, resulting in increased provision in 2020/21 and subsequent years of the framework</p>
Income	<p>Service Level Agreements with external users, application of appropriate debt policies (including, where appropriate, upfront payment for services delivered) and regular monitoring of income levels as a prompt to remedial action</p>
Legislative changes	<p>Provisions made in LTFFP and regular reviews of the adequacy thereof</p> <p>Ongoing monitoring of impacts of welfare reform on expenditure and income</p> <p>Active membership of relevant professional forums</p>
Legal claims and inquiries	<p>The Council explicitly provides for a number of known risks and liabilities. Funding could, however, be drawn down from the unallocated General Fund balance to meet unanticipated or additional costs</p>
Major infrastructure projects	<p>Regular progress monitoring through Change Boards, particularly at key milestones, with documented escalation procedures</p> <p>Senior Finance representation on all Project Boards</p>

## Projected Movement in General Fund

Appendix 2

	Projected Balance at 1.04.20 £000	Planned (Uses) / Contributions £000	Projected Balance at 31.03.21 £000	
<b>General Fund</b>				
<u>Balances Set Aside to Manage Financial Risks and for Specific Investment</u>				
Balances set aside for specific investment	32,854	(1,222)	31,632	Funding set aside for specific projects. Including monies for Enterprise Resource Planning, Local Development Plan and Tram Extension.
Contingency and Workforce restructuring	14,694	(2,000)	12,694	Monies held to cover costs of workforce management changes including staff severance costs, which may be utilised to support future change programmes.
Council Priorities Fund	571	(571)	0	Monies set aside from previous years' underspends which will be utilised to fund emerging Council priorities or expenditure pressures.
Dilapidations Fund	5,541	(175)	5,366	Monies set aside to meet costs arising from the termination of property leases and other related contractual commitments.
Insurance Fund	18,110	(1,000)	17,110	Insurance Funds are held to defray any loss where the Council could have insured against a loss but has not done so, and for paying premiums on an insurance policy. This includes the power to meet excesses on insurance policies and other claims arising from ongoing legal inquiries.



<b>General Fund</b>	<b>Projected Balance at 1.04.20 £000</b>	<b>Planned (Uses) / Contributions £000</b>	<b>Projected Balance at 31.03.21 £000</b>	
<u>Balances Set aside from Income Received in Advance</u>				
Licensing and Registration Income	3,016	(500)	2,516	Monies representing licensing income related to cabs, houses in multiple occupation, liquor and landlord registration. Council is not permitted to use these monies on other services.
Lothian Buses	504	0	504	Holds dividend income received from Lothian Buses which is being drawn down to support the Tram Extension project.
Other Minor Funds	143	0	143	Minor funds for other specific projects..
Pre-paid PPP monies and lifecycle costs	3,320	367	3,687	Monies set aside in recognition of the phasing issues related to grant monies, for lifecycle costs of projects.
Council Tax Discount Fund	3,131	500	3,631	Monies set aside as a result of reducing Council Tax second home discounts. Use of the fund is prescribed by the Scottish Government and is restricted to supporting the development of affordable housing. It forms part of the Strategic Housing Investment Fund (SHIF), alongside income from the Repairs and Renewals fund. The SHIF is fully committed to the delivery of new affordable homes by the Council and housing association partners over the next ten years and investment in services to reduce tenants' living costs. £12m was drawn down for this purpose in 2018/19 with a further £18m planned in 2019/20, with an estimated annual addition to the fund of £3m from Council Tax discounts.
Unspent revenue grants	461	0	461	Monies set aside at the year end, in accordance with proper accounting practice, where income has been received prior to the relevant expenditure being incurred. Funds will be drawn down in accordance with the grant conditions to match planned expenditure. The majority of funds will be drawn down in year and then new grant funding will be carried forward.

<b>General Fund</b>	<b>Projected Balance at 1.04.20 £000</b>	<b>Planned (Uses) / Contributions £000</b>	<b>Projected Balance at 31.03.21 £000</b>	
City Strategic Investment Fund	2,650	(1,300)	1,350	Funds set aside for strategic regeneration priorities £2.150m and £0.5m to provide match funding for new city development opportunities.
<u>Balances Set Aside for Investment in Specific Projects which will Generate Future Savings</u>				
Spend to Save Fund, Energy Efficiency and Salix CEEF	2,997	0	2,997	Funds set aside to assist service areas deliver revenue savings in future years through provision of one-off upfront revenue investment. Scheme repayments will be used to support further new initiatives.
<u>Balances Set Aside under Devolved School Management Scheme and Pupil Equity Fund</u>				
Balances held by schools under DSM / Pupil Equity Fund	5,500	0	5,500	Balances set aside for Devolved School Management Scheme and Pupil Equity Fund. There will always be a balance at March as the DSM scheme and PEF are based on an academic year.
<u>Unallocated General Fund</u>	14,072	145	14,217	Unallocated funds held against the risk of unanticipated expenditure and / or reduced income arising in any particular year, in line with Council reserves policy.
<b>Total General Fund</b>	<b>107,564</b>	<b>(5,756)</b>	<b>101,808</b>	