APPENDIX 2

SHORT TO MEDIUM TERM FINANCIAL STRATEGY

Background

1.1 The Short to Medium Term Financial Strategy forms part of a suite of documents used in the Council's financial planning:

- the three year budget reported when the budget for the year is set and regularly updated in reports to Council
- the indicative 10 year Capital Plan, underpinned by the Council's Capital Strategy
- the Council's Reserves Policy
- the Council's Charging Policy
- the Treasury Management Policy
- the Medium to Long Term Financial Plan
- sitting above all these the Council's Corporate Plan.

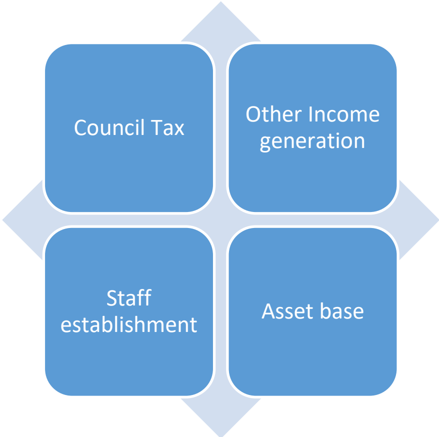
1.2 Moray Council in common with all other Scottish local authorities has been delivering service efficiencies and making budget savings for many years. Reserves have been used to make up the shortfall between the cost of services and funding for the Council. This is not a sustainable position. The Council therefore faces two challenges: to remove the reliance on reserves (the structural or underlying deficit in funding) and to contain budget pressures from increased demand or inflation within a reduced funding envelope from Scottish Government. These challenges become more difficult over time, with service efficiencies delivered and many services already reduced or removed.

1.3 When the budget for 2023/24 was set it was recognised that a very significant level of savings would be required over the period 2024/25 to 2025/26. That is the period covered by the Short-to-Medium term financial plan and strategy. The Council also has a Medium to Long Term Financial Plan, covering the period 2026 to 2033.

1.3 The update on short to medium term financial planning reported to Council on 28 June 2023 set out the approach being taken to identify savings and also longer-term potential remodelling of the council. This document is based on that work and sets out a strategy to achieve a balanced budget in 2024/25 and 2025/26 whilst also looking to the longer term to achieve a sustainable council.

1.4 The sizeable structural deficit in 2023/24 indicates the pressing need to achieve significant savings in as early a timescale as possible.

2 Key Financial Levers



2.1 These levers are the key to both the short to medium and medium to long-term financial strategies. Increasing income from Council Tax and other charges lessens the need to reduce expenditure on the main drivers for the cost of our services: staff and our asset base, and so can be used to help protect services. The movement from each of these levers impacts on the required movement from the others.

3 Hierarchy of Savings, Income and Transformation

3.1 The Council has an agreed Savings Hierarchy, with transformation of services as the preferred option, followed by income generation, thereafter service reduction / cessation. Service transformation has been ongoing since 2018 when the **Improvement and Modernisation Programme (IMP)** was first approved. This Programme was based on the Reform Matrix and a number of design principles which together aim to deliver a sustainable council.

Reform Matrix

Transformation (different service)	Centralise/ amalgamate in-house; Share services; Outsource/ Commission; ALEOs/Trusts
Redesign of services (i.e. efficiency – same service leaner/new approach)	Digital Services; Redesign Jobs; Streamline processes (e.g. contact centre, SharePoint, energy management); Rationalise asset base (including Schools, CATs); Simplify Governance
Redefine Services	Stop; Reduce; Community contribution / provision of services
Income generation and commercialisation	Charges; Sponsorship; Council Tax; Investment Portfolio; New services to compete with private sector; Sale of assets

3.2 The Savings Hierarchy is based on the Reform Matrix, but looks to prioritise the approaches available where transformation and complex redesign cannot deliver savings in the required timeframe.

3.3 The impact of strands of work being progressed under the Improvement and Modernisation Programme (IMP) has been included in successive budget projections and this is updated as these progress. There have been two iterations of IMP, with modest savings being generated to date and estimated savings from work underway incorporated in budget projections. A third programme is in development which also looks at how to transition to a council fit for the future – the **Future Council** - but the timeframe in which this will deliver savings is unlikely to have a significant impact in the span of the Short to Medium Term Financial Strategy.

3.4 Recognising the lead-in time for service transformation through IMP 3 is likely to impact most in the medium to long term, Heads of Service have been reviewing their services for what is being described as **Savings Max** for 2024/25 onwards – seeking to look for the maximum service income generation assessed as being achievable coupled with the maximum savings from cuts assessed as feasible in the short to medium term. Given that cumulative savings of £58 million have been taken from the budget over the past 13 years, some of the Savings Max options are unpalatable but the extent of the budget gap makes it unavoidable that these are considered and very serious cuts will have to be made.

3.5 In addition to the possibilities of services generating additional income, wider issues of income generation are included – referred to together as **Income Max** – and the main scope which the Council has to generate additional income is through increases to Council Tax. This is an important lever. During the period of the Council Tax freeze locally generated taxation revenue became an increasingly diminished feature of local authority funding. An element of growth in Council Tax would assist to start rebalancing the funding of Council services whilst also giving some protection from inflation. The 3% baseline assumption used over recent years in the budget dates from the Treasury target for inflation of 2% and is clearly out of step with the current economic climate.

3.6 These two elements of income and savings from cuts are included in the Budget on a Page appended as Appendix A (**APPENDIX 3** to this report). The Budget on a Page shows the funding gap and focusses on the various potential contributions to filling the gap, grouped thematically.

3.7 Looking at the elements set out in the Budget on a Page, potential savings from employer's pension contributions to the North East of Scotland Pension Fund are also included. It will be October before consultation on potential contributions commences and so no clear estimate is currently available. However, a saving of £1 million is included as a working assumption.

3.8 Also shown are some key themes which may generate early savings such as procurement and our Workforce Strategy.

3.9 Options looking at Council Tax as a measure to protect services are also set out reflecting potential increases similar to those agreed by some other councils in previous years. Increasing Council Tax by 1% generates around £0.5 million – to bridge the funding gap without the savings max proposals or using reserves would require an increase in Council Tax of 27%. To bridge the funding gap without savings but using covid reserves would require an increase in Council Tax of 8%. A combination of savings, a Council Tax increase and some limited use of reserves is therefore likely to be required in 2024/25 and this is picked up through the approaches set out in the Communications and Engagement Strategy agreed at Council in August.

Short to Medium Term Financial Strategy

4 The Funding Gap

4.1 On current estimates the Council needs to find savings of £16 million across the two year period 2024/25-2025/26. In both financial years it requires to set a balanced budget. The level of savings required are such that, depending on the way in which the levers described previously are used, these may not be achievable in one year. Use of reserves may therefore still form a limited part of the short term financial strategy. Consideration needs to be given however to the risks inherent in relying on reserves and the extent to which this is prudent. The strategy therefore assumes use of reserves will be kept to a minimum and is the last option to be brought into play when balancing the budget. Free general reserves are already at the policy minimum.

5 Proposed Strategy to Balance 2024/25 budget

5.1 The elements set out below follow the Council approved Savings Hierarchy (see paragraph 3.1):

Proposal	**Comment**	**Potential Scale**
Small scale transformation / efficiencies		
Energy saving measures	As set out in the Energy Strategy Report to the Economic Development and Infrastructure Services Committee on 15.11.22	Small £8,000-£10,000 pa
IMP 3 savings	High level estimate already included for IMP 1 and 2– main impact beyond 2025/26	
Other opportunities if any identified		
Income generation		
Council Tax	3% increase included in base – consider higher increase	Significant (£0.5m per 1%)
Council Tax	Scottish Government (SG) are consulting on increasing ratios for Bands E to H	Significant – would yield £0.75 million (if approved, may be phased in)

Proposal	Comment	Potential Scale
Council Tax on second homes	SG announced (Programme for Government) it will give powers to increase	Significant – up to £1 million
General increase in charges for services (excluding savings specifically identified in Income Max)	Annual review per Council policy	Small to medium – 1% increase on all discretionary charges would generate around £80,000
Further service reductions		
Continued review	Savings Max from service cuts	Significant - @ £4.6 million in total (Green and Amber)
Emergency temporary measures	Review of purchasing card activity Postpone capital projects from 2023/24 Halt service developments Delay recruitment Delay contract awards Temporary building closures	Likely to be small scale

5.2 Consideration of all the above options includes assessing the impact of the Council's statutory duties, the impact on the public, impact on other services of the Council, Equalities and Socio Economic Impact, risks to the Council and Workforce impacts. Conditions placed on Council funding by the Scottish Government are also an important factor as these restrict the Council's options.

6 Use of reserves

6.1 As stated, given the scale of savings to be found, an element of use of reserves to balance the budget in 2024/25 is anticipated. This must be kept to a minimum and planned and managed along with consideration of the costs of transition to a sustainable Future Council because, with only earmarked reserves and minimum free reserves remaining, any use of reserves simply adds to the savings required the following year and as such use of reserves in this way is not sustainable. Remaining Covid reserves by the end of 2023/24 are currently estimated to be £9.2 m. These reserves derive from windfall funding from Scottish Government arising from Barnett consequentials and Scottish Government have previously voiced the expectation that they will be used to cover budget pressures in the short term. These are the only reserves not currently earmarked for other essential purposes, and they can only be used once.

6.2 It is important to note that officers have estimated lead-in times for savings max/income max in broad terms – some of these may be optimistic. If covid reserves are fully utilised in 2024/25, flexibility to offset such delays is lost.

7 Proposed Strategy to Balance the Budget in 2025/26.

7.1 If, despite efforts to minimise their use, covid reserves are exhausted by the end of 2024/25 then the options the Council has to balance the budget the following year are to take further efficiencies generated by IMP3 if these can be identified and implemented by that point, to generate more income or to further cut services. However, following on Savings Max, opportunities for further cuts will be limited and so the emphasis would have to shift to Income Max.

7.2 With this in mind, consideration should be given during the budget setting process for 2024/25 to agreeing an income strategy for a three year period, encompassing both Council Tax and charges for services, the impact of which could then be seen clearly in the Short to Medium Term Financial Plan and also link into the Medium to Long Term Financial Plan. Some savings also have potential to be implemented on a phased basis.

7.3 In terms of IMP 3, a number of opportunities which may deliver early savings are in development:

- There may be opportunities to look at wider early income generation, for example related to renewable energy.
- There may be savings from procurement and energy efficiency measures.
- Use of Council assets needs to be reviewed, along with the condition of assets and their strategic location. Demographic projections will be relevant and the availability of data from the 2021 census will be useful in this regard. The review of the capital plan in 2023/24 will dovetail with this.
- Staffing in the widest sense should be considered, for possible savings ranging from further salary sacrifice schemes to changes in terms and conditions.

7.4 Horizon scanning will be important, to identify any legislation changes expected and likely impact of UK and Scottish Government plans.

7.5 The approach taken to identifying savings must align with the corporate priorities in the new Corporate Plan currently being developed and these priorities will be reflected in the Medium to Long Term Financial Plan.

8 Sensitivity analysis and budget assumptions

8.1 Key budget assumptions are set out below, with the impact of percentage variations on the budget projections

Budget component	Assumption	+/_ 1%	Impact on savings
Scottish Government Grant	Flat cash	+ / £2m	+/- 10%
Pay award	3%	+/- £1.6m	+/- 8.4%
Council Tax in-year collection	96.5%	+/- £0.6 m	+/- 3%
MIJB	Savings achieved and break even	+/- £0.5 m	+/- 2.6%
Loans interest	4%	+/- £2 m	+/- 10%

8.2 The projected budget is based on a number of other assumptions and these have been reviewed for potential risks to the Council or the budget setting process. Current recognised risks are;

- Based on current levels of expenditure, Moray Integration Joint Board may overspend on adult health and social care services. The Council is liable to contribute towards a share of any overspend
- There is a growing demand for Additional Support within Early Years and school settings. Additional funding has been allocated – this may prove insufficient; some funding is one-off – this may require to be converted to recurring funding
- Inflation is running at an elevated level for longer than anticipated at the beginning of the financial year – this is likely to lead to a higher than budgeted increase in the Real Living Wage and therefore to higher contract inflation in 2024/25 than currently budgeted for as well as creating pressures for pay negotiations.
- The Council is incurring significant unbudgeted costs for legal fees.
- The Council budgets for a mild winter in terms of winter maintenance but the actual cost will be higher if weather conditions are less good.

8.3 These and any other emerging risks will be kept under review as part of the short to medium term financial planning process.

9 Link with Medium to Long Term Financial Strategy

9.1 There are emerging proposals for transformation and for the Council of the future operating model which require to be assessed. Any proposals for the short term must be assessed against these emerging transformation proposals aimed to deliver the Future Council to ensure there is no significant conflict and they are aligned.

9.2 Looking at the transition from the short to medium to the medium to long term, the following elements set out earlier will together be key:

Income Max

What: Generation of income from Council Tax or by increasing current charges or introducing new charges

How: Savings hierarchy: income generation

Set current charges to highest tolerable level (a step change from the current very mixed observance of full cost recovery principle for locally set charges) and identify new charges that could be introduced. Tolerance will be judged by the overall level of income generated being increased and its role in bridging the gap relative to other levers, all in the context of and taking account of any impact on priority groups to ensure that the council's equalities and socio-economic duties being met.

Savings Max

What: Reductions in service budgets achieved through:

- Service redesign generating rapid efficiencies that enable the same service provision at less cost
- Redefining the service – reducing or stopping all or some of the service

How: Savings hierarchy: service savings and cessation.

Prioritised approach: to ensure that savings and remaining spend are consistent with council priorities, statutory and external requirements and constraints imposed on savings options (e.g. contractual issues, funding criteria from government)

Savings Max/Income Max:

Budget templates have been developed to show maximum possible savings to provide maximum possible scope to reduce costs from savings. Decisions will be required as to the extent of the whole package of savings to be taken and how to phase these for implementation to be manageable and deliver the savings in the necessary timing.

Transformation/IMP

What: Programme of work to support a financially sustainable council by delivering savings using the Reform Matrix of Transformation, Redesign, Redefine and Income Generation to identify projects and project management approaches to define and deliver.

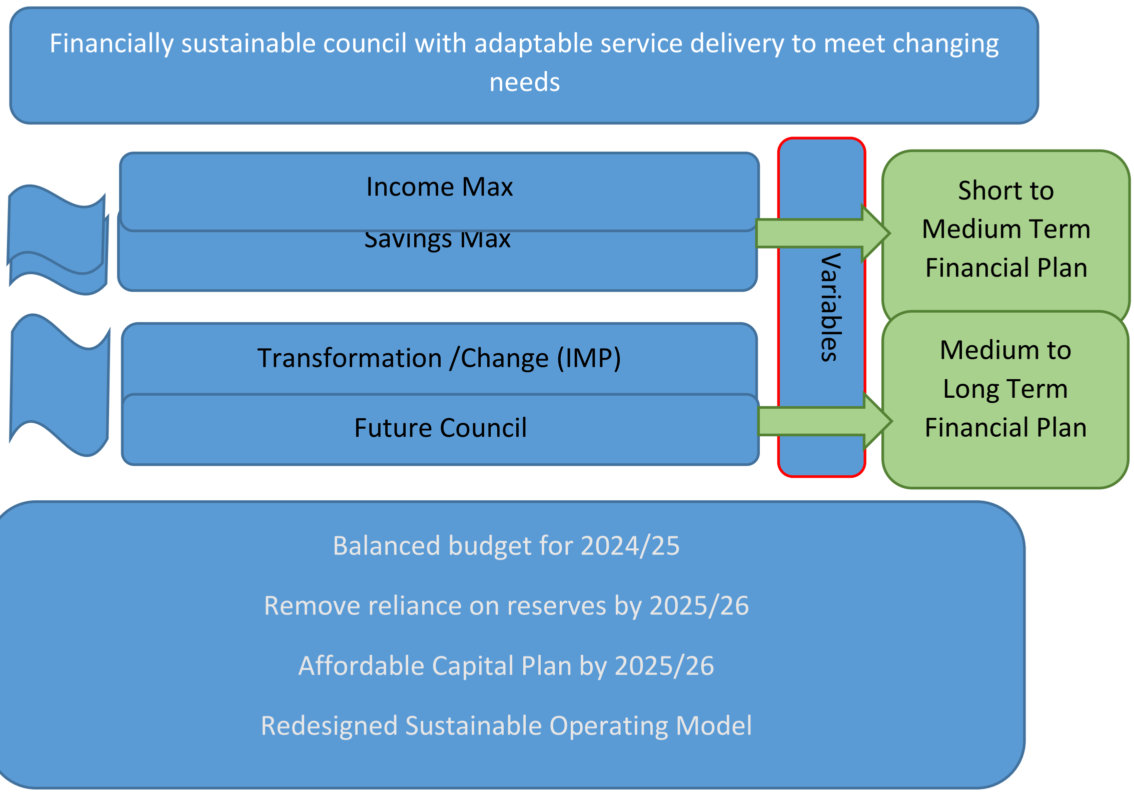
How: Savings hierarchy: transformation of services

Future Council

What: Identify and develop future operating model for council suited to council priorities providing adaptable future service delivery within sustainable balanced revenue budget and affordable capital plan.

How: Savings hierarchy: transformation of services

The interplay across these 4 elements is shown below leading from the overarching purpose to the ultimate objectives:



9.2 The Medium to Long Term Financial Plan is being drafted and will incorporate IMP3, which is in development. The Medium to Long Term Financial Strategy will be reported to Council in October.

10 Capital Plan Review

10.1 In tandem with the revenue focussed Short to Medium Term Financial Strategy set out above, a review of the capital plan has commenced. The review will:

- Reassess borrowing costs in the light of current interest rates
- Update medium to long term costs in the light of current cost estimates
- Identify an affordable capital envelope for the 10 year plan, using the local PI of a cap on financing costs as a percentage of total revenue budget

- Review plans for 2023/24 and 2024/25 to identify potential areas for delay / reduction.

10.2 The fourth bullet point directly ties into the Short to Medium Term Financial Strategy in that reduction in planned capital spend for 2023/24 and 2024/25 potentially delivers savings in financing costs for 2024/25.

10.3 Part of the capital review should be to consider the potential for reduction of the Council's asset base and this will be a strong theme in the Medium to Long term financial strategy.

10.4 The review also needs to consider the length over which planned programmes of capital expenditure will take place and the risks associated with various options, as deteriorating assets can require remedial revenue spend and the balance between capital investment and repairs and maintenance is an important consideration in asset management.

10.5 The capacity to carry out capital works from in-house resources must also be taken into account.

11 Other Factors

Other factors likely to directly affect short to medium term financial planning are as follows:

11.1 The Verity House agreement will need to be taken into account when further detail becomes available. Baselining of funding of itself is unlikely to give significant financial flexibility; that will depend on the removal of conditionality and spend reporting requirements. The main elements of conditionality in 2023/24 were funding for Integration Joint Boards and maintenance of teacher numbers and numbers of support staff in schools. Given the financial situation of Moray Integration Joint Board (MIJB), flexibility regarding funding for MIJB is unlikely to yield significant savings. The implications of the three shared priorities within the agreement will also affect what may be possible / desirable.

11.2 The potential emergence of other local tax raising powers and potential increase of council tax ratios for Bands E to H.

11.3 Updated data for Grant Aided Expenditure. Current projections appear to be that Moray will have a relative reduction in young people compared to Scotland as a whole and that will reduce our grant funding. However, previous census results have proven population estimates to be below actual and that has resulted in increased funding.

12 The Wider Context

12.1 The following are key considerations:

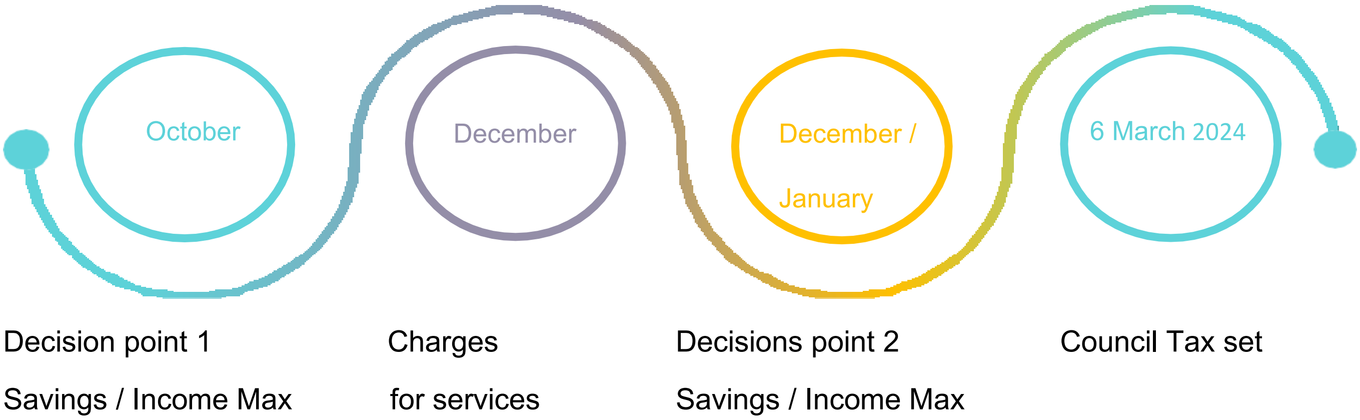
- Risks arising from increased inflation and interest rates, with likely impact on pay claims and general increases in prices across the board;
- Future funding, with Scottish Government finances under pressure and being targeted to specific priorities;
- Significant funding at UK and Scottish Government level coming from bid funds, requiring expertise and effort to access and with considerable monitoring

requirements;

- Demographic pressures and emerging social needs post pandemic;
- Significant difficulties in recruiting staff ;
- Moray Integration Joint Board (MIJB) is overcommitted against its budget and we will have to fund our share of any overspend. The long-term impact of the pandemic on MIJB services is as yet unknown;
- Our school estate requires significant investment to bring facilities up to the Scottish Government's recommended 'B-B' standard;
- The need to keep pace with wider digital transformation.
- Meeting our target of carbon neutral by 2030 will be a financial and technical challenge

13 Timescales and actions to implement the strategy

13.1 Savings Max to be set out as two-stage decision process:



13.2 Workforce consultation and public engagement require to be factored in, commencing August 2023 with high level communications and separate Workforce and Public Engagement Strategies in development.