

To: Executive Sub Committee

On: 01 June 2018

**Report
by
Director Scotland Excel**

Draft Funding Model Proposal

1 Introduction

This report provides an overview of potential future funding models for Scotland Excel.

2 Background

The *Revenue Estimates 2018-19* report presented at the Joint Committee on 8th December 2017 highlighted the challenging future financial landscape for local government and the impact on Scotland Excel. It recognised that over the medium term, local government in Scotland is likely to face further contraction in available resources, relating predominantly to the provision of revenue grant from the Scottish Government. In this context, Scotland Excel will continue to seek operational savings, to manage its financial position flexibly in order to maintain its aim of minimising the level of requisition required, and also to develop value propositions for member authorities to ensure that best value is achieved.

The report presented to the Joint Committee stated that “*the indicative medium term financial position, and includes an estimate that Scotland Excel will in 2019/20 (assuming no change in the level of requisition and no reliance on reserves) require to secure additional income or reduce costs by £168,000; rising to £254,000 in 2020/21.*” Additional analysis has been undertaken to review the deficit beyond this period and the pattern of an increasing gap continues in subsequent years (predominantly linked to assumed levels of pay award).

Throughout 2017/18, Scotland Excel has been reviewing opportunities and options to address the issue and to identify additional income. A number of successes have been achieved with projects generating additional benefits to members but each on a “cost recovery” model. Further investigation was sought

on the potential for projects to generate a surplus and the use of rebates and supplier levies.

The report presented to the Joint Committee in December 2017 concluded that *“It is likely that the solution to the funding gap outlined will consist of a blend of the options outlined above, along with continued focus on cost efficiencies and sourcing new associate member income in order to avoid increased requisitions. However, the possibility of a requirement for increased requisition income over the medium term cannot be ruled out. It is suggested that Scotland Excel further explore the options outlined above and bring a report back to the June 2018 Joint Committee meeting to provide an indication of how and in what timescale the above options could be implemented.”*

In addition to the operational deficit outlined at committee, there are other areas where ongoing funding gaps exist. The main area of concern is within the Scotland Excel Care portfolio. This report provides further information on the gaps within care and the options explored in order to try and diversify its funding base.

Care Portfolio

Members will be aware of the additional social care services that Scotland Excel has been providing to members encompassing Supported Living, Care at Home and Care Homes for Older People. Funding for these projects has been from Scottish Government funding or project specific additional member fees.

Scotland Excel has been exploring future funding options for these services and has discussed this with a wide range of stakeholders. A number of options have been explored including payment of additional member fees, introduction of rebates and levies and alternative funding sources such as Scottish Government.

To date, no consensus has been reached in this matter and the “funding gap” remains, as does the demand for these important services. In order to seek an alternative and perhaps more palatable funding method, Scotland Excel is examining if the additional sources of income outlined in this paper can be utilised.

The services are:

Care Home Services for Older People

Scotland Excel is leading on a wide portfolio of activity for Care Home Services for Older People including the development of a care cost calculator. The funding

for this project comes from annual contributions from 28 of the 32 Scottish local authorities (excludes Highland, North Lanarkshire, Orkney and Shetland). These contributions are confirmed 2019/ 2020.

Funding Received

Financial Year	Total
2017/ 2018	£173,198
2018/ 2019	£173,198
2019/ 2020	£173,198

It is anticipated that future funding requirements for this service will reduce based on lower resource requirements after the initial tender period. This is reflected in the forecast data provided later within this paper.

Care & Support Services

Care at home and supported living services are new areas of collaborative procurement activity for Scotland Excel. The 31 HSCPs across Scotland spend over £750 million per annum on these services, with no consistent approach to how these services are commissioned.

After engagement with key stakeholders, it proposed that Scotland Excel will develop a national, flexible framework for care and support services, incorporating both care at home and supported living services.

The Scottish Government has grant funded Scotland Excel to March 2019 to take this work forward. The funding was for a two year period only with a small amount of funding at the start of 2016/2017.

Funding Received

Financial Year	Total
2016/ 2017	£20,250
2017/ 2018	£154,750
2018/ 2019	£175,000

3 Funding Opportunities

A number of potential funding opportunities have been identified by Scotland Excel and explored further. They are as follows:

1. Consultancy Services
2. New Build Housing
3. Learning and development
4. Rebates
5. Associate Membership Expansion

A short summary on their background, financial scale and opportunity analysis is included below for each project. Each project has been submitted to our internal business development sub-group and more detailed evidence and criteria reviewed.

3.1 Consultancy Services

Background

Scotland Excel has historically undertaken a number of smaller scale consultancy projects within the sector. These have all been typically on a cost neutral basis. More recently, the organisation has targeted larger scale projects and recently was successful in its bid to support Fife council in their transformation programme and in this case, incorporated a small surplus.

This project will seek to develop and formalise the chargeable consultancy services that could be offered to members and the wider public sector including the affordable housing sector. No offering will be made beyond the public sector.

Chargeable services will be beyond the standard support provided to members as part of their core requisition.

Consultancy services will encompass areas such as:

- Provision of a benchmarking service to non-members.
- Undertaking a procurement exercise on behalf of another body.
- Provision of change services e.g. business improvement exercises.
- Transformation programmes of various scales.
- Bespoke exercises for members and non-members e.g. Options Appraisals.

Project Financials

Growth in this area has been limited in the past due to resources and strategy to focus on core members. Future projects will be costed based on full recovery of costs and the addition of a transparent and modest surplus.

Contribution to deficit

The project is anticipated to provide a financial return early in period 2019/20. A prudent approach has been taken to develop and grow this income stream over the coming years and is shown in table 1.

Table 1.

Fiscal	Surplus
2019/20	£70,000
2020/21	£70,000
2021/22	£70,000
2022/23	£80,000
2023/24	£90,000

Risks

Risks associated with this project are failure to make an entry into this market and failure to deliver to agreed and contracted commitments. Internal risks are also present including attraction and retention of suitable resources. Ongoing work is underway to address these potential risks.

Competition and competitive advantage

There is a high degree of competition in this market from both private and public sector. Competitors within the public sector include the Improvement Service, NSS and the Scottish Procurement Alliance within the housing sector. Scotland Excel feels it has a number of competitive advantages including:

- Existing knowledge and relationships with members and associate members.
- Not for Profit and Public-Sector status allowing a more open and transparent relationship with customers.
- Policy of sharing knowledge and retaining Intellectual Property within the public sector.
- Existing skill base and capability of Scotland Excel staff

3.2 New Build Housing

Background

In its Programme for Government 2017/18, the Scottish Government committed that 35,000 of the 50,000 new build houses to be constructed BY 2021 will be for

social rent. The commitment will deliver a 67% increase in affordable housing supply. Local government and the affordable housing sector will be required to undertake considerable procurement activity to meet this ambitious house building programme. After extensive stakeholder engagement, Scotland Excel has initiated a project to meet this procurement demand through a new funding approach.

This new funding approach provides this much needed framework with a number of additional benefits to the wider public sector and an additional financial return to those organisations investing in the project.

A detailed business case was presented to stakeholders and investing councils which provided all project costs, return on investment, project risks etc. Scotland Excel has elected to also invest in the project and will utilise the anticipated return towards the Scotland Excel deficit outlined above.

Project Financials

The project costs were calculated as £500k over a two year period. These project costs will be covered by the 12 investing councils including Scotland Excel.

Contribution to deficit

The project is anticipated to provide a financial return early in period 2020/21. A prudent approach has been taken to spend on the framework and is based on current knowledge of house build plans as published by the Association of Local Authority Chief Housing Officers (ALACHO). Currently Scottish Government funding has only been confirmed until 2021 therefore rebate estimates beyond this point have been based on lower historical build figures. It is anticipated, however, that funding and therefore spend will continue at the similar level rather than revert to these lower levels. The contribution to deficit is shown in table 2.

Table 2.

Fiscal	SXL Rebate
2019/20	£0
2020/21	£95,390
2021/22	£95,390
2022/23	£16,155
2023/24	£16,155

Risks

The main risk for the framework is that members choose not to utilise it once it is in place. Additional risks are related to the uncertainty of future Scottish Government funding of new build housing.

Competition and competitive advantage

A number of alternative frameworks are available within the market place including SPA, Scape and frameworks developed by individual local authorities and housing associations that are offered for wider use.

The Scotland Excel approach has a competitive advantage to these alternatives through a number of mechanisms including:

- Offering some form of specification/design standardisation to increase speed of development, realise efficiencies and ensure ease of use
- Offering standard templates/contract forms to ensure ease of use
- Encouraging the use of local suppliers/workforce via sub-contracting arrangements
- Providing a vehicle for the delivery and recording of community benefits such as apprenticeships
- Providing contract management activity

3.3 Learning & Development

Background

Scotland Excel has historically delivered an award-winning service to the wider public sector. In the past two years, the organisation has reviewed its strategy in this area and is now taking a wider, deeper and work-based approach to organisational learning. The creation of our new 5 year Learning and Development strategy has the aim of Scotland Excel being the public sector partner of choice for procurement and related disciplines. It takes a multi-disciplinary learning approach and learning programmes are currently segmented by procurement, leadership & management and project management.

Our new approach seeks to utilise internal capabilities, technology and strategic partnerships to deliver learning, additional member benefits and a financial return that can also support the organisational deficit.

Project Financials

The project costs have been integrated into delivery costs so that the project is self-sufficient. Investment for growth is reviewed on a regular basis and investment made when sufficient demand and tangible opportunities exist.

Contribution to deficit

The project is anticipated to provide a financial return in 2019/20 and is shown in table 3.

Table 3.

Fiscal	Surplus
2019/20	£53,000
2020/21	£53,000
2021/22	£55,000
2022/23	£60,000
2023/24	£62,000

Risks

There are a number of internal risks for the project around operational delivery but the team are confident these can be overcome. The main risk is that the wider public sector does not utilise the learning and development services due to budget constraints or other reasons such as mismatch between supply and demand. Scotland Excel has addressed this to-date by ensuring that costs are minimized, and tangible learning and development needs drive the development of a timely and effective offering. A further risk is the availability of suitable resource qualified to deliver against the portfolio of learning subjects.

Competition and competitive advantage

Competition for the Learning and Development offering comes from a number of areas including Higher Education, National Shared Services (NSS) and private providers. Scotland Excel has actively addressed this competition by seeking out gaps or strategic partnerships to optimise the service to the public sector.

The programme has a number of competitive advantage points:

- It has an established Academy with 4 active cohorts.
- Multi-disciplinary expertise across 3 major disciplines.
- Expanding portfolio - both the number of disciplines and the grade of qualification.
- The first Chartered Manager Assessment Centre in Scotland.

- The first CIPS accredited public-sector Procurement work-based-learning programme in Scotland.
- Benchmarked cost-effectiveness.
- Quick return on investment from the application of knowledge in work-based practice.

3.4 Rebates

Background

The use of volume rebates has been used to varying degree of success across the Scotland Excel portfolio to date. Some frameworks have had a rebate embedded within the commercial agreement, such as within construction materials, where others have offered successful returns on a one-off basis. A recent example of an effective implementation was the introduction of a new rebate in the contract for the supply and distribution of groceries. In this case, the rebate of c.£135k funded a team to deliver small value contracts, the delivery of which yielded a forecast efficiency of c.£700k from contracts delivered in the first year alone.

There are some challenges associated with the regular use of rebates as an income stream. These are largely associated with the lack of certainty within buying patterns, and the perception that suppliers will inflate prices to covered costs incurred. However, using historical data, coupled with an acute understanding of market conditions in which the sector operates, there is clear belief that this can be overcome. Additionally, there is also the view that if rebates are maintained at very modest levels, for example less than c.0.75%, there is no adverse effect on pricing.

It is the intention therefore to include a rebate review as part of the internal contract governance process, and consider applicability of the inclusion of rebates as standard practice going forward.

Project Financials

The inclusion and monitoring of contract rebates will be an integral part of the role of the contract manager. As such, it is not anticipated that this will attract additional overheads. However, going forward, there may be a need to supplement the current administration support to ensure an effective rebate recovery process is maintained.

Contribution to deficit

The project is anticipated to provide a financial return early in period 2020/21. It is provided in table 4.

Table 4.

Fiscal	Surplus
2019/20	£0
2020/21	£55,000
2021/22	£100,000
2022/23	£572,000
2023/24	£811,000

Risks

The main risks associated with this inclusion is lack of stakeholder buy in, both from councils and the market, and the lack of guaranteed sales volumes. These will be mitigated by wide customer and market engagement, and detailed analysis of previous buying patterns to enable effective forecasting of future demand.

Competition and competitive advantage

A number of buying organisations, both public and private sector, employ the use of rebates/supplier levies to generate income; as such, this is not a new concept. Also, given the significant purchasing power associated with local government collaborative activity, coupled with the low value by percentage planned to be introduced, it is not expected that this would introduce an additional threat to Scotland Excel as the partner of choice.

3.5 Associate Member Expansion

Background

This project will seek to take a much more proactive approach to the identification and enrolment of associate members to Scotland Excel. The project will make use of the existing affordable housing team to accelerate this within their sector. Additionally, the project will develop a model of associate support and development that supports core members, associate members and is productive for Scotland Excel.

A proposal to support this project will be made to the Joint Committee in December 2018. This proposal will seek to set out the legacy of the Affordable

Housing programme funded by Scottish Government until the end of this fiscal period.

Project Financials

The December 2018 proposal will demonstrate the growth in associate membership that financially supports ongoing associate growth and costs in order to provide a surplus towards the Scotland Excel deficit.

Contribution to deficit

The project is anticipated to provide a financial return in period 2019/20 and is contingent on acceptance of the future proposal. It is provided in table 5.

Table 5.

Fiscal	Surplus
2019/20	£50,000
2020/21	£55,000
2021/22	£55,000
2022/23	£60,000
2023/24	£60,000

Risks

The main risk for the project is failure of a sector to embrace the opportunity of associate membership or sectors where an alternative sector procurement provider is already present and imbedded. The strategic direction of Scotland Excel's frameworks will also set the potential direction for associate growth. The Scotland Excel Associate strategy sets out the markets that it would anticipate growth in.

Competition and competitive advantage

Scotland Excel's inherent strategy and ethos provides a number of key competitive advantage points:

- Offering a range of frameworks that are legally compliant with significant cost savings for potential associate members.
- Freeing up local resource spent tendering to allow greater focus on local service and core business
- Delivering standard terms and conditions
- Delivering cost savings and social value back into the local communities

- Provision of additional related services
- Provision of learning & development opportunities to new associate staff.

4 Review of Options

Office space

Section 3 of this paper outlines the additional services that can contribute towards the deficit faced by Scotland Excel. In order to facilitate this expansion, Scotland Excel must also review its existing office space.

Scotland Excel's primary office space is provided by Renfrewshire Council and is located within Renfrewshire House, Paisley. The office occupies 676 square metres of a wing on the fourth floor of the building. The remaining 247 square metres is currently occupied by a department of Renfrewshire council.

At the December 2017 Joint Committee, members agreed to extending the lease from February 2018 to February 2019. This one year extension was designed to allow Scotland Excel to consider options and to prepare recommendations for the Joint Committee.

The existing office space has been optimised to provide the maximum number of desks for staff. The organisation has implemented agile working including hot-desk facilities to increase its staff to desks ratio. Scotland Excel continues to work with colleagues at Renfrewshire council to continue this approach.

Initial work has been undertaken with Renfrewshire council staff to understand the possibility of expansion into the additional space and indicative costs have been provided. A proposal will be brought to the Joint Committee in June that will provide further information on this topic. To ensure members have a full picture of the 5-year forecast, indicative figures have been incorporated into the total funding gap.

Table 6 provides a summary of the total funding gap including the operating deficit (assuming a 2% pay award in each year), the care services and office expansion. It should be noted that the operational deficit figures for 2021/22 and beyond are clearly more difficult to ascertain and therefore proportionate estimates made.

Table 6

Project	Fiscal Period				
	2019/20	2020/21	2021/22	2022/23	2023/24
Operating Deficit	-£168,000	-£254,000	-£334,000	-£414,000	-£494,000
Care Home for Older People	£0	-£97,955	-£99,914	-£101,912	-£103,951
Supported Living and Care at Home	-£169,394	-£172,782	-£176,238	-£179,762	-£183,358
Proposed office expansion	-£50,000	-£50,000	-£50,000	-£50,000	-£50,000
Total	-£387,394	-£574,737	-£660,152	-£745,675	-£831,308

A number of options have been identified to address the deficit faced by Scotland Excel over the coming fiscal periods.

Option A – Efficiencies and Requisition

The introduction of efficiencies and potential member requisition increases was suggested as a possible route in the December 2017 Joint Committee report.

Scotland Excel continues to review its operating model for introduction of efficiencies that reduce operating expenses. This has been across all areas of the annual budget including staffing and secondary costs. 83% of the annual budget is on staff and 10% on the provision of premises and Service Level Agreements. Operational deliverables from staff have been a key focus for a number of years with increased services delivered from the core budget. Further work has also been undertaken with regard to premises and service level agreement. Scotland Excel will continue to review its operational model and seek the introduction of efficiencies.

Scotland Excel accepts and recognises that it is not palatable to increase requisition costs for members whilst the local government sector operates in an ever-challenging environment. Despite this it is important to consider the potential impact and contribution this would make to the deficit. Table 7 provides an indication of the potential impact of a requisition increase.

Table 7

Increase %age	Annual Contribution to Deficit
0.5%	£17,421
1.0%	£34,842
1.5%	£52,263
2.0%	£69,684
2.5%	£87,105
3.0%	£104,526

The table demonstrates a small range of increases and is not a recommendation on the nature or scale of a requisition increase. It is however apparent when considering the data provided in table 6 that requisition increases would have to be significant to alleviate the total deficit.

Option B – Income generation

This option is whereby Scotland Excel proceed with the projects outlined in section 3 and endeavor to develop a number of services/projects that provide an operating surplus.

The total forecasted annual contribution to deficit is shown in table 8.

Table 8

Project	Fiscal Period				
	2019/20	2020/21	2021/22	2022/23	2023/24
1. Consultancy Services	£70,000	£70,000	£70,000	£80,000	£90,000
2. New Build Housing	£0	£95,390	£95,390	£16,155	£16,155
3. Learning and Development	£53,000	£53,000	£55,000	£60,000	£62,000
4. Rebates	£0	£55,000	£100,000	£572,000	£811,000
5. Associate Member Expansion	£50,000	£55,000	£55,000	£60,000	£60,000
Surplus	£173,000	£328,390	£375,390	£788,155	£1,039,155

It is evident that despite the healthy and positive potential contribution that the five projects could add to meet the deficit, it is insufficient to cover the total deficit outlined in table 6 in the medium term. This is represented by table 9.

Table 9

Project	Fiscal Period				
	2019/20	2020/21	2021/22	2022/23	2023/24
Operating Deficit	-£168,000	-£254,000	-£334,000	-£414,000	-£494,000
Care Home for Older People	£0	-£97,955	-£99,914	-£101,912	-£103,951
Supported Living and Care at Home	-£169,394	-£172,782	-£176,238	-£179,762	-£183,358
Proposed office expansion	-£50,000	-£50,000	-£50,000	-£50,000	-£50,000
Total	-£387,394	-£574,737	-£660,152	-£745,675	-£831,308
Income	£173,000	£328,390	£375,390	£788,155	£1,039,155
Estimated surplus/deficit	-£214,394	-£246,347	-£284,762	£42,480	£207,847

Based on the above figures a different approach will be required to address the issue than solely income generation.

Option C – Hybrid approach to funding

Scotland Excel takes a hybrid approach to tackling the total deficit. This option incorporates the options presented in Options A, Options B and also suggests continuing the current arrangements for funding the older people care home work whereby participating councils fund this directly.

In both options demonstrated above, the deficits over 2019/20 to 2021/22 are the most immediate and difficult to resolve. The lag involved in the introduction of a number of the income generation projects and the growth in projected costs (mainly attributable to anticipated pay awards) results in a projected deficit position over the medium term.

A potential action to resolve this would be an increase in member requisitions. Further work is currently underway with Renfrewshire Council treasurer to understand the nature of this and to consider alternative approaches, potentially involving the flexible use of reserves and existing project funding. It is anticipated that the work on this will be complete in order to provide an update to the Joint Committee in June 2018. Any requisition changes will require to be formally agreed at the December 2018 Joint Committee. No assumptions on requisition increases have been incorporated into the financial modelling provided.

In addition to the above, the existing members who utilise and have provided initial funding for the Care Home for Older People service are asked to continue funding this work.

The results of this option are demonstrated in Table 10.

Table 10

Project	Fiscal Period				
	2019/20	2020/21	2021/22	2022/23	2023/24
Operating Deficit	-£168,000	-£254,000	-£334,000	-£414,000	-£494,000
Care Home for Older People	£0	-£97,955	-£99,914	-£101,912	-£103,951
Supported Living and Care at Home	-£169,394	-£172,782	-£176,238	-£179,762	-£183,358
Proposed office expansion	-£50,000	-£50,000	-£50,000	-£50,000	-£50,000
Total	-£387,394	-£574,737	-£660,152	-£745,675	-£831,308
Income	£173,000	£328,390	£375,390	£788,155	£1,039,155
Care Home for Older People - Member funded	£0	£97,955	£99,914	£101,912	£103,951
<i>Estimated surplus/deficit</i>	-£214,394	-£148,392	-£184,848	£144,393	£311,797

5 Next steps

It is apparent from the details in table 10 that further work is required to address the situation. Although the options highlighted in Option C go towards addressing the longer-term issue, they do not address the short to medium term forecast deficit.

Once a direction is agreed by members at the Joint Committee in June 2018, Scotland Excel will extend its existing work with key stakeholders to further communicate the approach and to provide assurances on the robust future financial performance of the organisation.

6 Conclusion/Recommendation

Scotland Excel has taken an ambitious and prudent approach to securing the financial sustainability of the organisation over the next 5 years. It anticipates that

in the same period, the organisation will see its contract portfolio rise from the current £1bn to £2.5bn which in turn will deliver further value and savings to members.

The organisation will also deliver a number of key services to members in order to support councils' wider ambitions and continue to be its partner of choice.

Committee members are requested to note and comment on the proposed approach to meeting the deficit whereby:

1. The funding opportunity projects are progressed by Scotland Excel.
2. The *Care Home for Older People* project continues to seek direct funding from the participating councils for 2020/21 and beyond.
3. Scotland Excel continues to work with colleagues in Renfrewshire council to identify methods to address the short-term deficit.
4. Scotland Excel will bring a paper detailing the solution to the June 2018 Joint Committee. This paper will document the approach that would be taken in the coming months in order to present a balanced budget to the December 2018 Joint Committee for approval.