

Money Matters
Financial Outlook for the County Council
Medium Term Financial Strategy &
Reserves as at 30th June 2018

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Lancashire

County
Council



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Financial Outlook for the County Council: Medium Term Financial Strategy

1. Executive Summary

At full council in February 2018 the medium term financial strategy (MTFS) set out a forecast funding gap of £144.084m by the end of the 4 year period (2018/19 – 2021/22). This report provides an updated position for the new 4 year period covering 2019/20 - 2022/23 and a review of assumptions to reflect the most current information available.

The updated funding gap is now reduced to £135.300m for the period 2019/20 – 2022/23. Improvements include an increase in council tax levels due to tax base increases and an improved council tax collection fund position. In addition savings relating to the Minimum Revenue Provision (MRP) agreed recently by Full Council have been included. Offsetting these improvements are in-year pressures resulting from a forecast shortfall in funding relating to capital receipts that had been assumed in the previous MTFS.

It is important to note that the funding gap is not evenly spread, with a varying gap over each of the 4 years as shown in Table 1. There remains significant uncertainty about the funding of the county council post 2019/20 as changes will be made resulting from business rates retention and the overall funding formula. These are amendments to the current funding system that are currently being developed and going through various pilot and consultation processes that the County Council is actively involved in.

The value of the uncommitted transitional reserve is currently forecast to be £125.009m by the end of March 2021 if there was no requirement for structural funding support from reserves to the 2019/20 or 2020/21 budgets. This represents an improved position from the £88.575m that was previously reported to full council in February due to a higher than forecast 2017/18 revenue underspend, a contribution to reserves reflecting a change in the Minimum Revenue Provision in 2017/18 and also some lower than forecast contributions from reserves to the revenue budget.

The impact of utilising the transitional reserve to fund the £60.596m gap in 2019/20 would leave a balance of £64.413m available to support the budget in 2020/21, however this will be insufficient to fully support the budget gap of £110.698m, requiring further savings to be made.

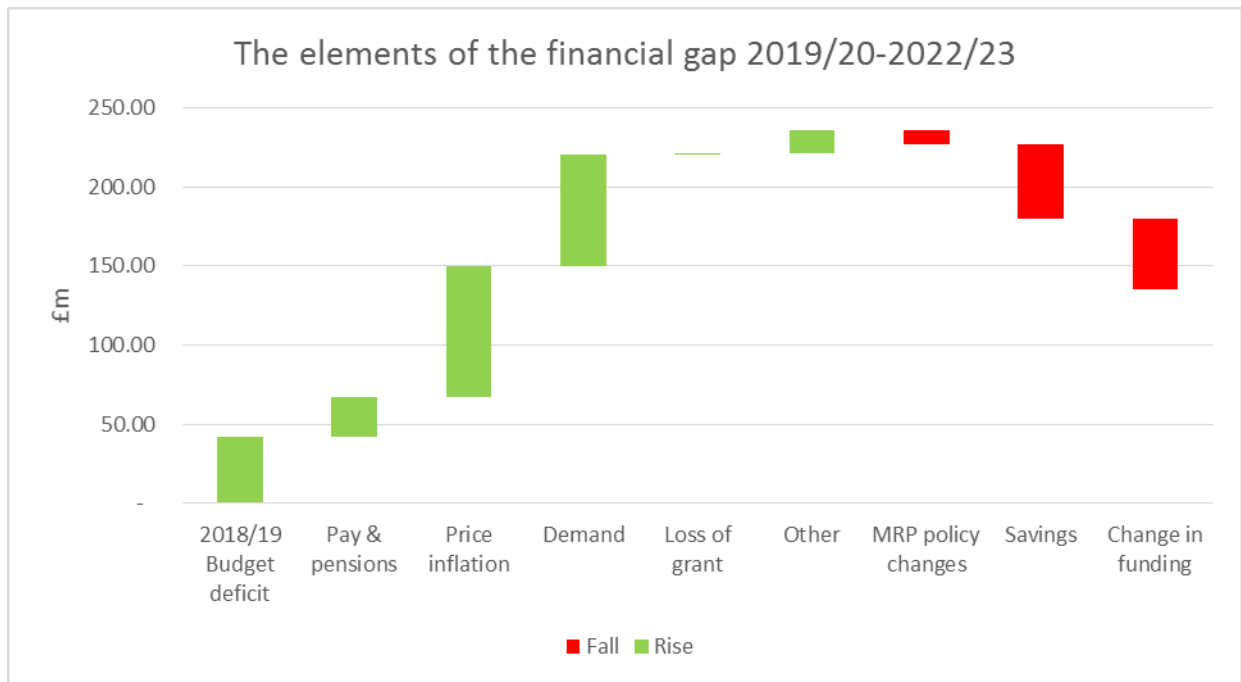
The table below provides a detailed analysis of movements between the previously reported financial gap and the revised financial gap:

Table 1

	2019/20	2020/21	2021/22	2022/23
	£m	£m	£m	£m
Forecast net budget requirement	800.877	813.550	803.558	0.000
Funding	774.512	763.822	777.612	0.000
Spending Gap as reported to Full Council February 18	26.365	49.728	25.946	0.000
Add change to forecast net budget requirement:				
Pay & Pensions	0.031	-0.544	-0.527	3.955
Inflation and Cost Changes	0.170	-3.094	-2.117	20.437
Service Demand and Volume Pressures	-0.577	0.093	-0.861	13.419
Other	-3.670	4.000	0.000	0.622
MRP Policy Change	-8.203	-0.183	-0.026	0.000
Specific grants	-0.300	0.000	0.000	0.000
Total change to forecast net budget requirement	-12.549	0.272	-3.531	38.433
Change to forecast funding:				
Funding	4.735	0.102	-10.782	-25.464
Reverse 18/19 use of reserves	42.045			
Total change to forecast funding	46.780	0.102	-10.782	-25.464
Funding Gap	60.596	50.102	11.633	12.969

Aggregated Funding Gap				
2019/20 (£m)	60.596	60.596	60.596	60.596
2020/21 (£m)		50.102	50.102	50.102
2021/22 (£m)			11.633	11.633
2022/23 (£m)				12.969
Total	60.596	110.698	122.331	135.300
Previous position (£m)	68.410	118.138	144.084	N/A
Variance (£m)	-7.814	-7.440	-21.753	N/A

The graph below demonstrates the drivers that make up the changes in the financial gap from £42m to £135m shown in the table on the previous page:



2. Funding

The funding included within this report reflects the final settlement that was announced on 6th February 2018. It is important to note that the proposed allocations issued by the government only cover the financial years up to and including 2019/20, therefore assumptions have had to be made for 2020/21 – 2022/23.

It is currently anticipated that a new system of local government finance will be in place in 2020/21 which involves local government retaining 75% of the business rates and a review of the funding formula. However, details of the scheme and the impact on Lancashire are not known at this time therefore the current business rates and grants structure has been forecast for future years, although it has been assumed that the revenue support grant will cease from 2020/21.

The figures above were based on a number of assumptions which have been revisited as part of this report and the latest information available has been included. The revised figures shown below show council tax increasing by 3.99% in 2019/20 and 1.99% thereafter, however this will be a decision made by full council each year when setting the budget.

The revised resources position incorporating the details set out below is as follows:

Table 2

	2019/20 £m	2020/21 £m	2021/22 £m	2022/23 £m
Revenue Support Grant	32.894	0.000	0.000	0.000
Business Rates	194.887	198.989	204.431	210.043
Council Tax	495.510	513.964	533.102	552.951
New Homes Bonus	3.472	3.019	3.010	3.010
Better Care Fund	40.014	40.014	40.014	40.014
Capital receipts	0.000	0.000	0.000	0.000
Collection Fund Surplus	3.000	3.000	3.000	3.000
Total	769.777	758.986	783.557	809.018
Funding - Previous MTFS	774.512	763.823	777.612	N/A
Variance	-4.735	-4.837	5.945	N/A
Impact on financial gap	4.735	0.102	-10.782	N/A

2.1 Council Tax and Business Rates

2.11 Council Tax

The MTFs currently has the following assumptions in relation to increases in council tax, however this will be a decision made by full council each year when setting the budget.

Table 3

	Council Tax increase (without the requirement for a referendum)	Additional council tax flexibility	Adult Social Care Precept	Total council tax increase
2019/20	1.99%	1.00%	1.00%	3.99%
2020/21	1.99%			1.99%
2021/22	1.99%			1.99%
2022/23	1.99%			1.99%

From 2020/21 onwards, it is assumed the maximum increase that the county council is able to apply to council tax is 1.99%, as the option to raise an adult social care precept will no longer be available, and the additional 1% flexibility without the requirement for a referendum is also not permitted post 2019/20. Council tax increases are subject to a full council decision each year when setting the budget, and any decisions taken not to increase council tax as per the assumptions above would increase the financial gap.

If the additional flexibilities such as 3% social care precept and additional 1% flexibility without the requirement of a referendum were applied in 2020/21 this would result in additional income of c£20m and would significantly reduce the financial gap. The adult social care precept was introduced pending the green paper on future funding of adult social care which has been delayed and there is no current indication of when funding solutions may be put in place.

Analysis of Lancashire's tax base over recent years indicates an average council tax base increase of 1.7%, therefore compared to the previously assumed increase of 1.5% this has now been built into the MTFs, generating an increased income of c£1m each year.

Council tax collection rates vary across district councils but are currently relatively low for Lancashire compared to other councils nationally. The county council is therefore working with some district councils to look at what steps could be taken to try and improve collection levels, as an increase of just 1% overall would increase funding levels of the county council by c£5m each year.

2.12 Business Rates

As shown in Table 2 business rates income is a significant portion of funding to local authorities. The baseline is an assessment of the business rate income required to meet service needs. For the county council, the amount anticipated to be received

from the business rates collected in the area is less than its assessed need, therefore it receives a top up grant.

Business rates income for the county council is heavily dependent upon cooperation from the district councils, and much will depend on the general economic performance of local areas. The collection rates across Lancashire present a mixed performance when compared nationally, therefore the county council is working with districts to improve this performance. In addition, there are valuation appeals outstanding, some of which are on large value properties. If successful these will have a negative impact on the ability to generate business rates. With this in mind a minimal amount of growth has been built into the local share (0.5%).

The county council is currently part of a business rates pool with 10 district councils across Lancashire. The Government has recently released a prospectus opening the application process for local authorities to apply to be a business rates pilot for 75% retention. There is currently work underway across Lancashire to assess the viability, risks and financial benefits of a pilot, which is currently offered as a one year opportunity before the new system is rolled out across all councils.

2.13 Collection Fund Surplus

The county council has reported collection fund surpluses since 2014/15, therefore based on the evidence of the previous 4 years an additional £3m of funding has been built into the anticipated funding levels. Previously collection fund surpluses have been treated as additional one-off amounts which have been added to reserves however given the evident recurrent nature of the surplus, this has now been added into the budget at what is felt to be a prudent and realistic value.

2.2 Capital Receipts

From 1st April 2016 the government introduced the flexibility for capital receipts to be used to fund revenue expenditure which meets certain criteria i.e. it needs to relate to activity which is designed to generate ongoing revenue savings or to transform a service which results in revenue savings or improvements in the quality of provision.

As part of the Provisional Settlement in December 2017 it was announced that flexibility to use capital receipts to help meet the revenue costs of transformation programmes will continue for a further three years.

The MTFs previously included £8.475m in 2019/20 and £9.672m in 2020/21. These amounts were forecast to be received following the development of the Cuerden site however, as the future of this site is not yet clear, the forecast capital receipts have been taken out creating a non-recurrent additional pressure on funding in those years. We fully expect a receipt to be forthcoming from the Cuerden site however the timing at this stage is unclear and once this is established the revised capital receipts will be built back in.

3. Net Budget Requirement

The MTFS covers spending pressures including pay increases, contractual inflation, increased demand for services and the impact of previously agreed and new savings measures.

3.1 Pay and Pensions

In December 2017 it was announced by the National Employers for Local Government Services that, following negotiations a new pay offer covering the period 1 April 2018 and 31 March 2020. In 2019/20 the new pay offer proposes that local government organisations move to a new pay spine and this is reflected within the pay budget requirement in the MTFS. A 2% increase has therefore been included in 2019/20 and an assumption of 1% included in later years until further information is known in relation to the pay spine and subsequent increases.

In March 2017 cabinet agreed to a re-profiling of the council's pension contributions resulting in a saving over a 3 year period. This is reflected within the MTFS based on the latest information available in relation to the county council's estimated contribution rate and deficit contributions.

The apprenticeship levy was introduced in April 2017 at a rate of 0.5% of an employer's pay bill, therefore an estimate of £1.323m was been included in the MTFS for 2019/20 with increases equivalent to the pay increase rates quoted above.

The table below presents the amounts built into the MTFS for pay and pensions:

Table 4

	2019/20 £m	2020/21 £m	2021/22 £m	2022/23 £m	Total £m
Employee Costs	10.272	4.186	3.890	3.567	21.915
Pensions Costs	0.374	0.374	0.374	0.374	1.496
Pension Prepayment Saving	-0.319	2.299	0.000	0.000	1.980
Other pay related costs	0.071	0.013	0.014	0.014	0.112
Revised Pay and Pension requirements	10.398	6.872	4.278	3.955	25.503
Pay and Pensions - previous MTFS	10.367	7.416	4.805	0.000	22.588
Impact on Financial Gap	0.031	-0.544	-0.527	3.955	2.915

3.2 Price Inflation and Cost Changes

Contractual price increases represent a significant cost pressure to the county council. The assumptions have been subject to regular review by services with an incremental reduction of £5.041m identified when comparing the values within the previous MTFS (2019/20 – 2021/22) and £20.437m included in 2022/23 to reflect the additional year.

Table 5

	2019/20 £m	2020/21 £m	2021/22 £m	2022/23 £m	Total £m
Adults Services	15.060	16.360	12.380	13.147	56.947
Children's Services	1.296	1.221	1.237	1.698	5.452
Waste Services	0.177	2.353	3.215	3.295	9.040
Other Services	3.592	2.793	2.546	2.297	11.228
Revised price inflation requirements	20.125	22.727	19.378	20.437	82.667
Price inflation – previous MTFS	19.955	25.822	21.495	0.000	67.272
Impact on Financial Gap	0.170	-3.094	-2.117	20.437	15.396

Some of the key areas of price pressure are:

- Adults services represents the most significant inflationary price pressure and forecast increases are based on future increases in fees paid being at 2018/19 levels. It is important that the county council keeps up with increases in the price of resources for providers to ensure the required service provision is delivered within a stable market.

The revised inflationary pressures included in this MTFS for adults services reflects a decrease of £4.599m when comparing the 3 years (2018/19 – 2020/21). This is based on the 2017/18 outturn position, and a review of those areas that do not require an inflationary uplift but which have previously been uplifted within the MTFS. The table also reflects an additional year's price inflation to reflect the inclusion of an additional year within the MTFS of £13.147m.

- Waste disposal continues to require significant budget to meet inflationary commitments over the next four years. This requirement has increased by £1.877m due to transport costs, and a new full year cost of £3.295m for 2022/23.
- Children's social care is a further significant area that requires price inflation within its budget. This includes items that will inflate such as agency payments, residence orders, foster and other allowances and payments to the health sector. This requirement has reduced by £0.202m and a new full year cost of £1.698m for 2022/23.
- Other smaller areas of price inflation include premises running costs, transport costs, concessionary travel, highways, winter maintenance, energy and legal fees.

3.3 Demand Pressures

All services have reviewed the demand pressures they face in future years and whilst they have reduced overall increasing demand still remains a significant element of the funding gap. The MTFs at quarter 1 forecasts decreased requirement of £1.345m when comparing those years contained within the previous MTFs, and a new full year demand pressure of £13.419m for 2022/23.

Table 6

	2019/20 £m	2020/21 £m	2021/22 £m	2022/23 £m	Total £m
Adults Services	13.531	15.831	9.473	10.163	48.998
Children's Services	7.139	3.056	1.668	1.415	13.278
Waste Services	1.764	1.824	1.931	2.058	7.577
Other Services	0.417	0.230	0.263	-0.217	0.693
Revised Demand Requirements	22.852	20.941	13.335	13.419	70.546
Demand – previous MTFs	23.429	20.848	14.196	0.000	58.473
Impact on Financial Gap	-0.577	0.093	-0.861	13.419	12.073

- Adult social care represents a large proportion of the demand pressures. Adult Social Care has long seen annual increases in the demand for services and the MTFS attempts to predict growth in future years largely based on reviewing current and past activity trends but also taking into account future population changes. From "a social care perspective" demand covers both increasing numbers of people eligible for support and the increasing complexity of those cases.

All demand assumptions contained within this revised MTFS regarding adult social care have been reviewed based on the most up-to-date trend analysis. There is a decrease to the forecast demand requirements across adults services at quarter 1 based on the 2017/18 outturn position across services.

- The cost of children's social care continues to experience increasing demand and has been increased again as part of this update of the MTFS. The assumption remains though that demand will ultimately plateau in future years, with a reducing demand increase built into the later years of the MTFS.

The demand pressures included in this MTFS for children's services reflects an increase of £2.719m when comparing the 3 years (2019/20 – 2021/22). The previous MTFS included reduced demand growth in future years, and the current update still makes assumptions relating to reduced demand increases in future years, however the pressure has had to be increased to reflect the 2017/18 outturn position and quarter 1 monitoring position. The table also reflects an additional year's demand pressure of £1.415m for 2022/23. This will continue to be monitored and reviewed.

- The revised MTFS continues to include a significant amount in relation to waste services demand pressures, with an increase of £0.898m when comparing the 3 years (2019/20 – 2021/22) that were in the previous MTFS. The position also reflects an additional year's demand pressure of £2.058m for 2022/23.

3.4 Other

This reflects a small increase in grants that are expected in children's services and also the impact of the non-recurrent benefit in 2019/20 of the final year of transitional improved better care fund (iBCF) funding.

3.5 Minimum Revenue Provision (MRP) Policy Change

The major adjustment in the MTFS for this category of expenditure relates to the recent revision to the MRP Policy that was agreed by full council. This has resulted in a budget reduction of £8.2m in the 2019/20 budget.

4. Reserves

Table 7

Reserve Name	Opening Balance 2018/19	2018/19 Expenditure	2018/19 transfers to / from other reserves	2018-19 Transfers from revenue budget	2018/19 Forecast Closing Balance	2019/20 Forecast Spend	2020/21 Forecast Spend	Total as at 31 March 2021
	£m	£m	£m		£m	£m	£m	£m
County Fund	-23.437	0.000	0.000	0.000	-23.437	0.000	0.000	-23.437
SUB TOTAL - COUNTY FUND	-23.437	0.000	0.000	0.000	-23.437	0.000	0.000	-23.437
Strategic Investment Reserve	-3.765	0.740	1.679	0.000	-1.346	0.850	0.350	-0.146
Downsizing Reserve	-13.891	3.346	5.941	0.000	-4.605	4.605	0.000	0.000
Risk Management Reserve	-5.402	3.449	-0.816	0.000	-2.769	1.169	0.800	-0.800
Transitional Reserve	-155.066	50.641	-10.579	-11.025	-126.029	0.826	0.194	-125.009
Service Reserves	-19.118	11.044	3.775	0.000	-4.298	2.753	0.762	-0.784
Treasury Management Reserve	-10.000	0.000	0.000	0.000	-10.000	0.000	0.000	-10.000
SUB TOTAL - LCC RESERVES	-207.242	69.221	0.000	-11.025	-149.047	10.202	2.106	-136.739
Schools/Non-LCC Service Reserves	-16.521	1.599	0.000	0.000	-14.922	-1.017	-1.020	-16.959
SUB TOTAL SCHOOLS/NON LCC RESERVES	-16.521	1.599	0.000	0.000	-14.922	-1.017	-1.020	-16.959
GRAND TOTAL	-247.201	70.820	0.000	-11.025	-187.406	9.185	1.086	-177.135

The county fund shown at the top of Table 7 is the balance set aside to cover the authority against a serious emergency situation (e.g. widespread flooding); a critical and unexpected loss of income to the authority and for general cash flow purposes. In considering these various factors the county council is forecast to maintain its County Fund balance at £23.437m.

The table above shows that the forecast value of the uncommitted Transitional Reserve is currently £125.009m and whilst it is anticipated that further revenue savings for 2019/20 and beyond will be identified, the impact of utilising the Transitional Reserve to fund the £60.596m gap would leave £64.413m available for use in 2020/21 based on current forecasts (as shown in Table 8). Work continues on the identification of savings, primarily through the completion of service challenges being undertaken

for all services with the outcomes to be brought to the December Cabinet meeting for decisions to be taken.

Table 8

	2019/20 (£m)	2020/21 (£m)
Transitional Reserve Opening Balance	126.029	64.607
Contribution to MTFS Funding Gap	60.596	64.413
Commitments	0.826	0.194
Transitional Reserve Closing Balance	64.607	0.000

5. Future Risks and Opportunities

The following are key future risks, the full impact of which is not known at this stage:

5.1 Agreed Savings Plans Delivery

The scale of agreed savings (£130m in 2018/19 – 2020/21) is significant and there are inherent risks in their delivery. Any significant under-delivery will create an additional funding pressure and impact on the ongoing and longer-term financial health of the council. This has been identified as one of the highest risks in the risk and opportunity register. There are comprehensive arrangements in place to track delivery of financial savings and take corrective actions where required.

A savings delivery programme of this scale always has some inherent risks relating to the speed of delivery, particularly where they are directly linked to reducing the future demand for services. Where services are experiencing a potential negative variance in their savings plans the service managers are actively seeking to meet any shortfalls through other activities within their service area.

5.2 Identification of Further Savings Opportunities

A process to identify further savings, referred to as the service challenge process, is well underway with each service across the county council presenting opportunities for further savings. A benchmarking exercise across all county councils (and other councils where appropriate) has identified that there are some service areas where Lancashire is higher cost, and therefore the process is aiming to deliver services at the median costs or below. The service challenges are scheduled to be completed by early November 2018 and the outcomes and related savings proposals will primarily come to cabinet for a decision in December 2018.

5.3 Business Rates Retention / Changes to Funding Formula

In 2015 the Chancellor announced that local government as a whole would be able to keep 100% of business rates by 2020 and this would be accompanied by clarity around what new responsibilities this would fund along with a revised national funding formula which could have a significant impact on the council's future funding base. This process has been delayed and has also now been revised to 75% business rates retention, with a current prospectus inviting applications for councils to pilot the scheme with a closing date at the end of September. There is currently a system of redistribution (top-ups and tariffs) to reflect there are councils with relatively higher needs but lower income from business rates and vice versa.

The county council currently receives a top-up grant, primarily as a result of having adult social care responsibilities, and although work is progressing nationally, with a number of complete and planned consultations regarding the changes, there is currently insufficient information available to model what the financial impact of the changes will be overall and specifically to the county council. Currently the forecast is assuming the ceasing of revenue support grant in 2020/21 and a relatively neutral position on business rates and formula funding thereafter.

5.4 Children's Social Care

Children's social care demand levels are forecast to continue to increase, particularly within agency residential placements, agency fostering placements and also special guardianship orders. Although the rate of growth is quite volatile, over recent months the rate of growth has slowed down slightly.

Significant additional budget was allocated to children's social support improvements and demand pressures over the past 3 years. An assumption within this MTFS is made that demand will plateau in future years, with a reducing demand increase built into future year's budget.

Since the last MTFS report the service has received the outcome of the recent Ofsted inspection which resulted in an improved rating of "requires improvement" and is working on the improvement implementation plan which will further inform the forecasts of future service demands.

5.5 Troubled Families Funding

The county council currently receives funding towards working with troubled families. Within the MTFS funding levels that we have received written confirmation for are included, but post 2019/20 there is no information available as to whether this funding will continue. It is therefore currently assumed that funding levels will remain at 2019/20 levels. If the funding does cease this will result in a pressure on the budget of £2.1m. Given the lack of clarity we have discussed this with other Local Authorities in a similar position, as to the approach they are taking, and they have confirmed that they are also forecasting the funding to continue, but this will be closely monitored as announcements relating to funding are made in the Autumn, and outcomes reflected in future MTFS reports.