Appendix C

Money Matters
Financial Outlook for the County Council
Medium Term Financial Strategy

Lancashire County Council

Financial Outlook for the County Council: Medium Term Financial Strategy

1. Executive Summary

1.1 Introduction

This report updates the financial position facing Lancashire County Council over the period 2015/16 to 2020/21. The County Council is experiencing an ongoing period of unprecedented financial pressure as a result of the Government's extended programme of austerity combined with significant increases in demand for public services.

Cabinet have received reports in August and November 2015 on the MTFS to cover the period 2015/16 to 2020/21. The latest reported funding gap over the five year period was £262.0m.

Since the last report in November 2015 the Secretary of State has announced the Provisional Local Government Finance Settlement for 2016/17.This report considers the impact of the Settlement on the MTFS, the impact of budget decisions taken by Cabinet and updates other assumptions in light of current information. As a result of these reviews the funding gap has reduced to £200.5m.

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m	Total £m
Funding gap reported to Cabinet – November 2015	**90.174**	**21.940**	**56.018**	**47.592**	**46.283**	**262.007**
Impact of Settlement	21.577	8.849	-15.210	-4.319		**10.897**
Impact of Expenditure Pressures	-3.402	5.276	2.271	2.341	1.496	**7.982**
Saving options Cabinet November	-64.177	-0.687				**-64.864**
Funding Decisions						
Council Tax increase in 2016/17	-15.515					**-15.515**
Capital receipts application	-5.000	-7.500	7.500	5.000		**0.000**
Business rate pooling	-0.400	0.400				**0.000**
Revised Funding Gap	**23.257**	**28.278**	**50.579**	**50.614**	**47.779**	**200.507**
Change in Funding Gap	**-66.917**	**6.338**	**-5.439**	**3.022**	**1.496**	**-61.500**

1.2 Conclusion

Lancashire County Council continues to face, as previously stated, an unprecedented period of financial constraint through to at least 2020/21.

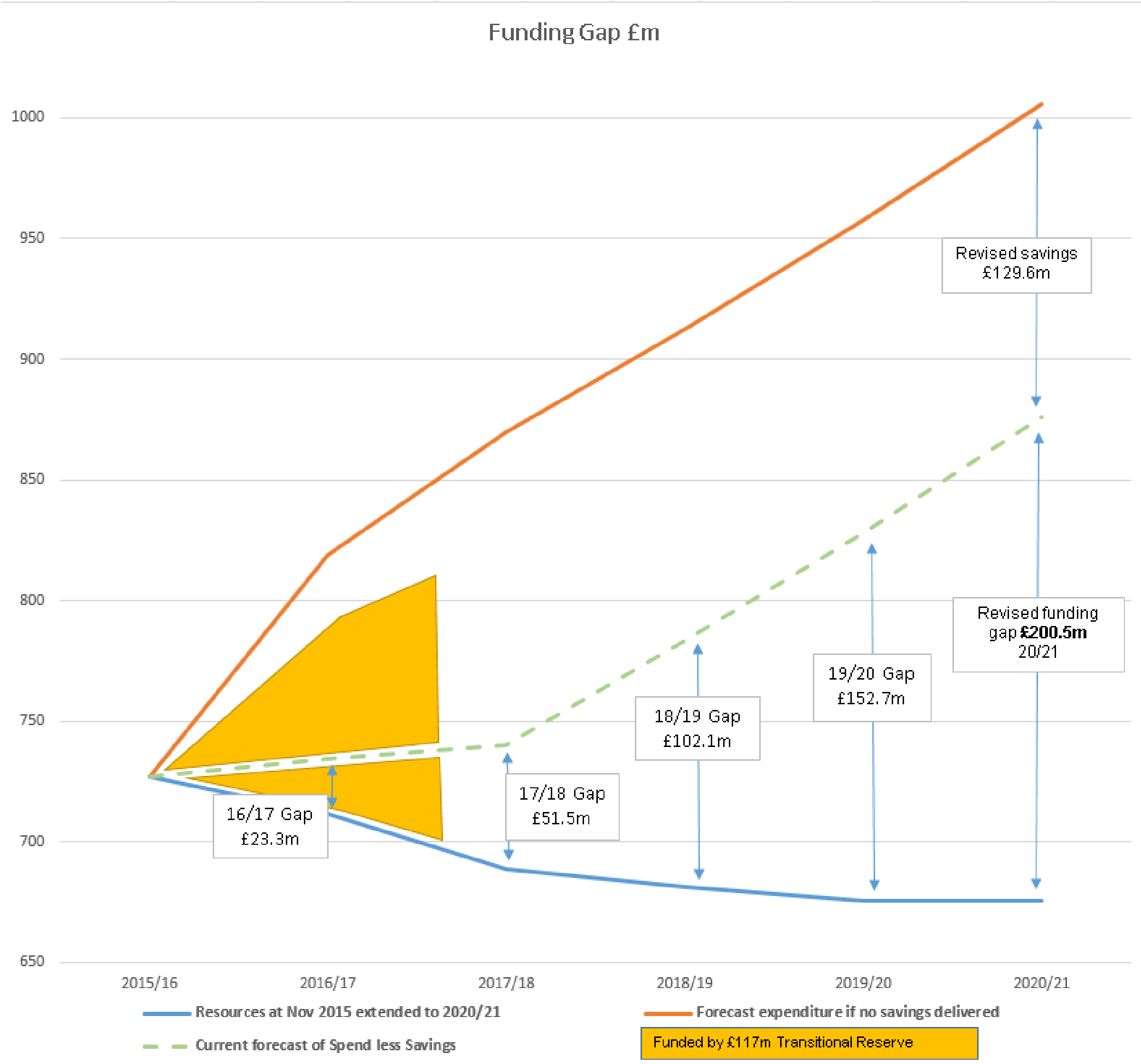
The financial commitment required to fund statutory demand led services is almost certain to result in using up all available resources. The resource available for discretionary services will be minimal (if any exists at all) and at this stage we cannot be certain of the point at which funding may not cover statutory demand led services as the resources have yet to be confirmed. However, indications from the initial base budget review suggest that there will be insufficient resources to cover statutory services from 2017/18.

The County Council, in redesigning the services it provides to the public, faces the challenge of doing so whilst delivering further savings of an estimated £200m over the next 5 years.

As part of the process of redesigning its services the County Council has recognised that it will need to utilise its reserves. Details on the reserves are detailed in the Money Matters report Appendix B. In this report it is noted that as at 1 April 2015 the County Council had reserves of £328.7m of reserves; some of which are already committed. Including the Funding Gap identified in this report, it has been identified that there is an estimated reserves requirement of £145m to support the revenue budgets in 2016/17 and 2017/18. Consequently, by 31st March 2018 it is expected that there will only be the £36m County Fund and a residual £20.613m of service reserves. All other reserves will have been spent.

The graph below illustrates the potential use of reserves compared to the funding gap requirement over the period. The element of the funding gap that can be funded from reserves is highlighted. This indicates that reserves will not be available to fund the gap beyond 2017/18, by which point it is estimated that all available reserves will have been used. The graph has four components:

- The red line shows the current estimated total expenditure that the County Council would incur if no savings were made.
- The dotted green line shows the anticipated level of expenditure the County Council would make if the current savings targets were achieved. Our current savings plans do not fully address the decreasing resources. The graph shows the cumulative gap that will accrue year-on-year if further savings are not made resulting in a £200.5m funding gap by 2020/21.
- The blue line shows the current estimate of resources available to the County Council which decreases over time.
- The shaded area represents the proposed use of the £117m Transitional Reserve. Some of this reserve has already been committed to fund the cost of savings taken out of the budget but which will not be made immediately (as agreed by Cabinet in November). It is important to note that there are insufficient reserves to finance both these commitments and the funding gap in 2017/18.



2. Resources

The County Council's previously reported MTFS assumes a 7% reduction in government funding in both 2016/17 and 2017/18 and reductions of 6% in 2018/19 and 2% in 2019/20. These were based on information on Government Departmental Limits .

These assumptions provided the following forecast of resources available to the Council which were included in both the August and November MTFS reports.

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m
Level of resources	705.034	684.221	668.977	663.781	663.926

These resources consist of:

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m
Council Tax	388.834	391.024	392.028	393.047	394.069
Business Rates	179.933	185.320	190.116	195.056	200.144
RSG	131.353	102.887	81.833	70.678	64.713
New Homes Bonus	4.914	4.990	5.000	5.000	5.000
Total Estimated Resources at November 2015	**705.034**	**684.221**	**668.977**	**663.781**	**663.926**

2.1 Provisional Local Government Finance Settlement December 2015

The Secretary of State issued the provisional Local Government Settlement on 17th December which provided details of support to local authorities for the next four years. In particular the Settlement covered details on the:

- Settlement Funding Assessment
- A new Better Care Fund
- New Homes Bonus
- Use of Capital receipts
- Council Tax increase limitations
- Business Rates Pooling

2.2 Settlement Funding Assessment (SFA)

The Settlement Funding Assessment (SFA) is a measure of the income that will be received from Business Rates and Revenue Support Grant (RSG). From the 2015/16 SFA (adjusted to reflect change in grants included within the SFA) to 2019/20, the County Council's SFA is showing a reduction of £117.7m (34.7%).

	2015/16 (adjusted) £m	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m
Settlement Funding Assessment (SFA)	338.466	292.249	258.326	239.014	220.747
Funded by:					
RSG		118.841	81.508	56.979	32.894
Business Rate baseline		173.408	176.818	182.035	187.853
TOTAL		**292.249**	**258.326**	**239.014**	**220.747**
In year reduction of SFA		**-46.217**	**-33.923**	**-19.312**	**-18.267**

A comparison of the SFA in the November MTFS with the settlement SFA is shown in the table below:

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m
November MTFS SFA	307.111	285.613	268.476	263.107
Settlement SFA	292.249	258.326	239.014	220.747
Variation	**-14.862**	**-27.287**	**-29.462**	**-42.360**

2.3 Impact on the Medium Term Financial Strategy

The County Council's previously reported MTFS had assumed that there would be a reduction in government funding. The assumptions made in the MTFS were a 7% reduction in government funding in both 2016/17 and 2017/18 and reductions of 6% in 2018/19 and 2% in 2019/20. The actual reductions in the Settlement are greater than those assumed.

The impact of these changes on the MTFS are shown overleaf:

	2016/17	2017/18	2018/19	2019/20
% change of SFA currently in MTFS	-7.0%	-7.0%	-6.0%	-2.0%
Actual SFA reduction	-13.7%	-11.6%	-7.5%	-7.6%
Impact on MTFS Funding Gap (£m)	**14.862**	**12.425**	**2.175**	**12.898**

2.4 Care Act 2014 Funding

From the details available it would appear that the Care Act funding is included within the SFA from 2016/17; hence an adjusted 2015/16 SFA has been calculated for comparison purposes. In the MTFS there is specific grant funding of £7m and therefore it is assumed that this has now been included in the SFA and represents a loss in each of the years having an overall impact on the funding gap of £7m.

2.5 Better Care Funding

The Secretary of State acknowledged in his statement that there are expenditure pressures arising from adult social care. It was therefore confirmed that there would be £1.5bn for local authorities to support work with health authorities to complement the Social Care Precept. In total this is expected to generate an additional £3.5bn for social care by 2020.Those council's with lower ability to generate council tax income will receive higher allocation. The County Council's allocation is as follows:

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m
MTFS	0.000	0.000	0.000	0.000
New Better Care Fund	0.000	3.210	22.656	40.014
Impact on MTFS Funding Gap	**0.000**	**-3.210**	**-19.446**	**-17.358**

2.6 New Homes Bonus

The Settlement includes an actual New Homes Bonus figure for 2016/17 and indicative allocation for 2017/18 to 2019/20. These future years' are lower to reflect a reduction in the total funding allocated in future years'. However, the New Homes Bonus System is subject to change and actual allocations will depend upon the outcome of the consultation and also the impact of future local growth. Using the indicative allocations will have the following effect on the MTFS:

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m
MTFS	4.915	4.994	5.000	5.000
Settlement assumption	5.084	5.531	3.475	3.333
Change	0.169	0.537	-1.525	-1.667
Impact on MTFS Funding Gap	**-0.169**	**-0.368**	**2.062**	**0.142**

2.7 Use of Capital Receipts

As part of the Autumn Statement the Chancellor of the Exchequer announced that the rules for the use of capital receipts, which is the income received from the sale of the County Council's fixed assets, were to be amended to help local authorities deliver more efficient and sustainable services. Currently the use of capital receipts is restricted to the funding of capital expenditure or the repayment of debt. From 1 April 2016 it is proposed that capital receipts can be used to fund revenue expenditure which meets certain criteria.

To meet the qualifying criteria the revenue expenditure needs to be on any project which is designed to generate ongoing revenue savings or to transform the service so as to make savings or improve the quality of service provision.

Local authorities will only be able to use capital receipts from the sale of property, plant and equipment received in the years in which this flexibility is offered. They may not use their existing stock of capital receipts to finance the revenue costs of reform.

Current estimates of the capital receipts to be generated are:

	2016/17 £m	2017/18 £m	2018/19 £m
Capital receipts generated	5.0	12.5	5.0

Provided suitable expenditure can be identified an estimated £22.5m can be applied to the revenue budget although this will have an impact on the Capital Programme which will either have to be reduced or be funded from an increased level of borrowing.

It should be noted that the receipts are one-off resources and there is a possibility that the level of receipts to be generated from the sale of assets will not be maintained at these levels for a sustained period of time. The actual receipts received in any one year will fluctuate in line with local property markets and the type of asset available for sale. Therefore, there is a risk that in any given year the receipts actually received will be less than assumed and therefore the situation will be monitored closely.

The funding gap shown in section 1.1 already assumes the use of these receipts. This is subject to the approval of the recommendation that the capital receipts are applied to revenue as outlined above.

2.8 Council Tax increases

The Council Tax referendum limit set by the Secretary of State remains at 2%. However, as an authority with social care responsibilities the council tax can be increased by up to 4%, providing that 2% is used for social care. If Lancashire were to increase the Council Tax for 2016/17 by 3.99% then it is estimated that an additional £15.515m would be generated.

Based on an estimated tax-base then the Council Tax position would be:

Council Tax cash 2016/17	£404.361m
Tax base	344,178.24
Band D Council Tax 2016/17	£1,174.86
Band D Council Tax 2015/16	£1,129.78
% increase between 2015/16 and 2016/17	3.99%

Details on the actual Council Tax-base will not be finalised until February and the above is an estimate of the council tax and the estimated cash generated in 2016/17.

The funding gap in section 1.1 assumes an increase in the Council Tax of 3.99% is applied but this will be subject to decision taken by the County Council.

2.9 Business Rate Pooling

The Settlement includes government assumptions of the amount of business rates individual authorities require to fund their services (the baseline funding). When the business rates retention system was implemented in 2013/14 the concept of a levy was also introduced. This levy was due to be paid to central government when a local authority's increase in revenue from business rates outstrips the increase in its baseline funding level.

Although the system calculates data for individual authorities there was the option for local authorities pooling between themselves subject to the approval from the Secretary of State. This arrangement is beneficial as it would enable more of the levy to be retained locally. A Lancashire Business Rate Pool was approved for 2016/17 covering the County Council and nine of the Lancashire Districts. It is currently estimated that the County Council will receive £0.4m additional income in 2016/17 as a result of the pool.

2.10 Summary of Potential Funding Changes on the MTFS

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m
Resources Previous MTFS	705.034	684.221	668.977	663.781	663.926
Change in SFA	-14.862	- 27.287	- 29.462	- 42.360	-42.360
New Better Care Fund		3.210	22.656	40.014	40.014
New Homes Bonus	0.169	0.536	- 1.525	-1.666	-1.666
Capital receipts available	5.000	12.500	5.000		
Council Tax increase 2015/16	15.515	15.515	15.515	15.515	15.515
Business rate pooling	0.402				
Updated Resources	**711.258**	**688.695**	**681.161**	**675.284**	**675.429**
Change in year	**6.224**	**4.474**	**12.184**	**11.503**	**11.503**
Impact on MTFS Funding Gap	**-6.224**	**1.750**	**-7.710**	**0.681**	**0.000**

3. Net Spending Pressures

The MTFS covers spending pressures including pay increases, contractual inflation, increased demand for services and the impact of previously agreed savings measures that are either no longer achievable at all or not to the scale or in the timeframes originally planned**.**

3.1 Pay

In the July Budget the Chancellor announced a 4 year restriction on public sector pay increases at 1% per year. Using this as a guide the MTFS has included an assumed pay award of 1% for each of the years with the cost shown below. This assumption is unchanged since August.

However, a recent court case has concluded that holiday pay for those who work regular overtime should be based on overall pay, including overtime, and not just basic pay. To accommodate this change £0.648m relating to affected staff has been included as a new recurrent cost pressure.

These pressures are summarised in the table below:

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m	Total £m
Impact of 1% pay award	2.3	2.3	2.4	2.4	2.4	**11.8**
Holiday pay costs	0.7					**0.7**

The Chancellor also announced increases to the minimum wage for people aged over 25, referred to as the 'National Living Wage'. This is completely separate to the Living Wage the County Council is committed to paying its employees as an accredited member of the Living Wage Foundation.

Since the last MTFS the Living Wage Foundation has announced a 5% increase in its Living Wage. This is greater than initially anticipated. The impact of having a 5% annual increase and the impact of more grades being incorporated into the Living Wage is being examined. An initial assessment of the costs show that the MTFS needs to be increased as follows:

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m	Total £m
Impact of Living Wage	0.624	1.464	0.923	0.979	1.039	**5.029**

These costs are currently being reviewed in the light of more up to date information and are subject to change.

This does not include the impact of any regrading required to maintain wage differences nor the impact of any of the budget options. This wage differential between grades is a significant risk. If the County Council was required to maintain the differentials there would be a significant additional cost. An initial exercise to ascertain the cost indicates an additional £11m per year would need to be found.

3.2 Price Inflation

Contractual price increases represent a significant cost pressure and initially there was an estimated cost over the period of £106.5m. The assumptions have been subject to regular review by services and a reduction of £15.4m was identified in November. Within this MTFS there has been an increase in the price inflation £1.7m identified from 2016/17 bringing the total price inflation in the year to £92.8m.

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m	Total £m
Total price inflation	22.9	16.5	16.5	17.4	19.5	**92.8**
Impact of revised price inflation assumptions	1.7					**1.7**

Some of the key areas of price pressure are:

An estimated £58m over the period for payments to external providers of social care attract annual inflation in order for the fees paid by the County Council to keep up with increases in the price of resources for suppliers. The County Council has a legal responsibility to demonstrate the suppliers are able to deliver services with the fees paid to them. The inflation assumptions used for externally provided social care are set out below and are based on the application of relevant inflation rates to a costing model:

Service	2016/17	2017/18	2018/19	2019/20	2020/21
Nursing Care	2.5%	2.7%	2.9%	2.9%	2.9%
Residential Care	2.6%	2.9%	3.0%	3.1%	3.1%
Domiciliary Care	2.5%	2.6%	2.7%	2.7%	2.7%
RPI	2.2%	3.0%	3.1%	3.1%	3.1%

- £12.3m for the provision of waste disposal over the period of the MTFS.

- £5.6m on children's social care including agency payments, residence orders, foster and other allowances and payments to health. The payments to the health service are assumed to be at 1% in line with the pay award while the agency payments are capped at 2% per annum. Other allowances are generally at 2.2%.

3.3 National Living Wage

In his budget in July the Chancellor announced the introduction of a new National Living Wage for all workers aged 25 and over. This was included as a risk in the previous report but reflects compulsory rates that organisations must pay their staff beginning with a rate of £7.20 per hour from 1st April 2016. It is anticipated that this will rise incrementally each year to at least £9 per hour in 2020 and is a cost pressure that has been recognised as significant nationally.

Whilst the impact of the newly announced National Living Wage has no impact on the costs already forecast for the Council's own employees due the Living Wage Foundation impact outlined in 3.1, it is expected to impact significantly on the rates paid to providers of Adult Social Care commissioned services. It is now estimated that the County Council will incur additional costs over the period of £34.6m due to the implementation of the National Living wage. These have now been built into the MTFS position.

3.4 Demand Pressures

All services have reviewed the demand pressures faced by the County Council in future years. The impact of this review has been identified and is reflected in the revised MTFS and it can be seen that a significant proportion of the funding gap that has been identified is due to demand pressures.

In total it is estimated that the demand pressures are £97.4m. This is unchanged from the MTFS reported in November.

	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m	2020/21 £m	Total £m
Total demand pressure	38.4	12.7	13.9	15.0	17.4	**97.4**

In total, Adult Social Care represents approximately 70% 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 past activity trends but also taking into account future population changes.

In deriving the estimated cost of demand the following projections have been used:

- Older People – population projections from the ONS for the aged over 85 population.

	2016/17	2017/18	2018/19	2019/20	2020/21
Total Older People Population Projection Growth	2.86%	2.78%	3.30%	3.49%	4.21%

- Physical Disability services continue to see increases in the demand for direct payments, where service users receive a cash payment from the County Council for individuals to arrange their own care in place of the County Council commissioning services on their behalf. The average annual growth in Direct Payments for those with physical disabilities over the last 3 years has been 5.5%. As such, an annual increase of this amount has been included in the forecast.

- Learning Disability services has traditionally seen growth in service user numbers of around 3% per annum. The last reliable year of activity information shows a 3.7% increase in the number of people with community based support which makes up the majority of current expenditure for those with learning disabilities. As such a 3.7% increase per annum has been included in the MTFS.

- For Mental Health services the average annual increase in service user numbers in the last 3 to 5 years has been used across Residential, Nursing, Home Care and Direct Payment services to project increased spending over the period.

- As the demand for services increase, so does the increase for formal social care assessment to identify whether an individual has eligible care needs which would entitle an individual to financial support from the County Council to meet their care needs. Population increases in the over 85 population has been used to project forward spending growth in relation to assessment and care management staff.

- The cost of children's social care demand is estimated to be £13.4m. This covers the cost of population changes and the anticipated increase in the number of children in care. In addition, £5m relates to an initial estimate of the additional social worker capacity requirement reflecting additional demands and the potential impact of the Ofsted inspection, already built into the MTFS.

3.5 Loss of specific grant

The County Council receives various grants which are specific and form part of the net expenditure pressures rather than the general resources of the authority referred to in section 3 above. The County Council was subject to an in-year reduction to the Public Health Grant of £4.3m in 2015/16. It was anticipated that this will be a continuing reduction and was included in the November MTFS.

As noted in section 2.3 the Care Act monies has now been included in the general finance settlement and therefore this represents a loss of specific income of £6.885m.

3.6 Savings and Cabinet Decisions

The savings to be achieved are constantly under review. Previous MTFS reports identified £48m of savings that were considered not achievable. This includes £2.4m identified in November. No further changes to prior year agreed savings have been identified.

In November, Cabinet approved new budget reductions of £64.177m in 2016/17 and £0.687m in 2017/18. It was approved that officers were authorised to proceed with their implementation subject to consultation where appropriate, and that the 2016/17 budget be prepared based upon these revenue decisions be agreed, with the outcome of any consultations being reported to Full Council. The MTFS now incorporates these reductions.

3.7 Capital Financing Requirements

The budget options approved by Cabinet in November included a reduction of £7m to reflect a proposed change in the policy of calculating the Minimum Revenue Provision (MRP). Further work has been undertaken on the capital financing requirement taking into consideration:

- potential implementation of the new MRP policy,
- the impact on the capital financing budget from a change in the timing of the estimated rise in interest rates provided by the authority's external Treasury Management advisors,
- Cash-flow implications of the budget proposals and the use of reserves,
- The latest estimates of the Capital Programme and the requirement to borrow**.**

Given the latest estimates of interest rates, cash-flow and the Treasury Management Strategy regarding the taking of long term fixed debt it is estimated that there is a further reduction in the 2015/16 budget could be made. However, it is estimated that the costs will rise after this point. The impact on the MTFS is:

	2016/17 £m	**2017/18 £m**	**2018/19 £m**	**2019/20 £m**
MTFS change	-5.685	3.812	1.348	1.362

4. Future Risks

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

4.1 Better Care Fund

The budget currently includes £20m of income from the Better Care Fund. This will only be received if it is annually re-agreed by the 6 Lancashire CCGs. It is currently assumed that this will continue in the MTFS.

4.2 Deprivation of Liberty Safeguards

The Deprivation of Liberty Safeguards (DoLS) was implemented on 1 April 2009. It provides a legal framework for preventing the unlawful detention of anyone over the age of 18, in a care home or hospital, who lacks the capacity to consent to their care arrangements and residence.

Since March 2013 Lancashire County Council has taken the responsibility for assessment of people who meet DoLS criteria in hospitals as well as residential care homes and due to a Supreme Court ruling many more people are covered by the regulations. If the legal duty was rigidly applied revised estimates suggest that up to £5m could be the recurrent cost of full compliance. This has not been factored in to the MTFS.

4.3 Education Services Grant (ESG)

The Chancellor of the Exchequer announced in his Autumn Statement £600m savings from Education Services Grant as the government reduces the local authority role and statutory duties with schools. ESG is approximately £16m in Lancashire but as yet there has been no detail on the likely loss of resource to the County Council.