

Money Matters
Financial Outlook for the County Council
Medium Term Financial Strategy &
Reserves as at 31st December 2019

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Lancashire

County
Council



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1. Executive summary

At cabinet in January 2020 the medium term financial strategy (MTFS) set out a forecast funding gap of £28.438m by the end of the 4 year period (2020/21 – 2023/24).

This report provides an updated position covering the 2020/21 – 2023/24 financial years.

A review of assumptions, relating to both income and expenditure, has been undertaken to reflect the most current information available. Due to the ongoing and unprecedented uncertainty in relation to future local government funding there are a significant number of variables leading to a range of different funding scenarios. These were considered by the Corporate Management Team during Q2 and the most likely scenario was selected. This funding scenario remains the most appropriate and is the basis of this MTFS. The selected scenario is supported by advice from leading experts in local government finance and funding.

The updated funding gap contained within the report is £33.312m by 2023/24 which is an increase of £4.874m from the previously reported position. There is currently a forecast provision of £4.045m in 2020/21 to support the organisational improvement journey review work which is currently underway. The main reasons for the changes to the position are as follows:

- Revised estimates of the effect of indexation on the Revenue Support Grant.
- An update to the forecast of the funding available as a result of our pooling arrangements reverting to the 50% business rates retention scheme following the 75% pilot.
- The reflection of the 6% increase in National Living Wage which has an impact on the cost of provision of commissioned adult social care.
- Updated forecasts on pay and pensions following the completion of the latest triennial pension scheme valuation.
- Following a review of current activity, updated demand and volume assumptions.

The overall position over the 4 year period indicates a structural deficit of £33.312m by 2023/24, which varies over each of the 4 years shown in Table 1. Work is progressing on phase two of the service challenge process which will seek to address the ongoing deficit and is focusing on a number of cross-cutting work streams and areas for investigation identified in the initial phase, but where further work is needed to robustly evidence the scale and form of proposals. In particular, service challenge phase 2 is focused on the complex levers required to create an environment where service configuration and operational practice reflects best in class and supports demand management which is the single biggest driver on our costs. Further saving proposals will come forward for consideration at future cabinet meetings.

In arriving at the revised funding gap it has been necessary to make assumptions about future funding levels and there remains significant uncertainty about this past 2020/21 with changes to be made in respect of business rates retention, the overall funding formula, the anticipated green paper on adult social care and, of course, any government spending review.

The value of the uncommitted transitional reserve is currently forecast to be sufficient to meet the identified funding gaps beyond the period of this MTF5, which provides time to address the structural deficit in a considered and sustainable way. The intention remains to identify continued savings and deliver a financially sustainable position for the council.

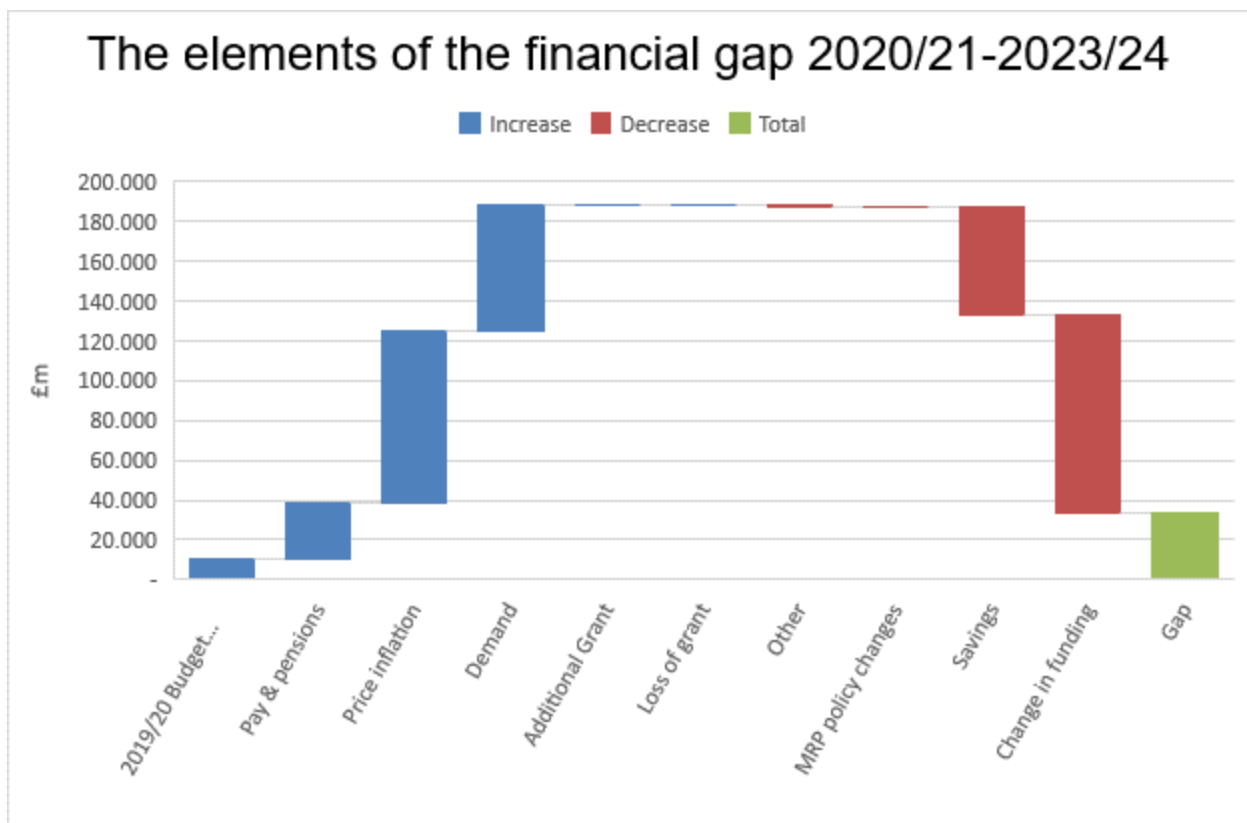
The table below provides a detailed analysis of movements between the previously reported financial gap and the revised financial gap:

Table 1

	2020/21 £m	2021/22 £m	2022/23 £m	2023/24 £m	Total £m
Spending Gap as reported to Cabinet	0.000	-5.188	14.150	19.477	28.438
Add change to forecast of spending:					
Pay & Pensions	-1.195	0.222	-0.042	0.385	-0.630
Inflation and Cost Changes	2.104	-0.216	-0.209	-0.057	1.622
Service Demand and Volume Pressures	-1.874	-0.999	-0.565	-0.917	-4.355
Other	0.372	0.204	-0.144	0.000	0.432
Additional Grant	-3.098	1.147	1.070	0.881	0.000
Loss of Specific Grant	0.000	0.000	0.000	0.000	0.000
Undeliverable Savings	0.000	0.000	0.000	0.000	0.000
Additional Savings	0.000	0.000	0.000	0.000	0.000
Re-profiled Savings	0.100	0.100	0.100	-0.300	0.000
Total change to forecast of spending	-3.591	0.458	0.210	-0.008	-2.931
Change to forecast of resources:					
Funding	-0.453	10.463	-0.812	-1.393	7.805
Total change to forecast of resources	-0.453	10.463	-0.812	-1.393	7.805
Funding gap	-4.045	5.733	13.548	18.076	33.312
Forecast net budget requirement	838.598	864.199	893.550	920.330	
Funding	842.644	858.467	880.003	902.256	

Aggregated funding gap	2020/21	2021/22	2022/23	2023/24
2020/21 (£m)	-4.045	-4.045	-4.045	-4.045
2021/22 (£m)		5.733	5.733	5.733
2022/23 (£m)			13.548	13.548
2023/24 (£m)				18.076
Total	-4.045	1.688	15.236	33.312
Previous position (£m)	0.000	-5.188	8.961	28.438
Variance (£m)	-4.045	6.876	6.275	4.874

The graph below demonstrates the drivers that make up the changes in the financial gap from £10.245m carried forward from 2019/20 to the cumulative position of £33.312m in the financial year 2023/24 as shown in the table above:



2. Funding

The funding included within this report reflects the provisional settlement for 2020/21 that was announced on 20th December 2019. The announcement confirmed that there would be a one year settlement in 2020/21 and that the fair funding review would be delayed until April 2021. There are no funding levels confirmed post 2019/20. Assumptions have therefore been made based on the provisional finance settlement for funding levels from 2020/21 – 2023/24.

Spending review, fair funding formula and 75% business rates retention

During 2020, a multi-year spending review will take place which will allow more time for the impact of funding changes to be effectively planned for.

The provisional settlement confirmed that 2020/21 would effectively be 'rolled over' from 2019/20, giving councils the stability they need to set a budget.

In the provisional settlement, the Chancellor announced that councils will have access to new social care funding of £1.5bn in 2020/21. This consists of grant funding and up to a 2% adult social care precept.

The provisional settlement also confirmed that revenue support grant would continue at 2019/20 inflated amounts, and that the social care funding allocated in 2019/20 would continue into 2020/21. It was also confirmed that the 2019/20 75% business rates pilots would not continue into 2020/21

As a result of the uncertainty of future funding during Q2 we carried out some scenario analysis around possible funding profiles. In total 9 scenarios were modelled (this is not an exhaustive analysis of all funding options but consisted of the most obvious measures which could be taken) which resulted in forecast funding gaps between a surplus of £6m to a deficit of £85m. Following a review of these scenarios by the corporate management team, including the consideration of advice from external advisors, a core and most likely funding scenario on which to base this medium term financial strategy was agreed and this scenario remains the most appropriate for this MTFS.

As a result of the above the assumptions around funding are that:

- Revenue support grant or funding at the equivalent value through any new fair funding formula will be ongoing for the currency of this plan
- An adult social care precept of 2% will be levied in 2020/21 only
- The social care grant announced in the provisional settlement will continue for the length of the parliament which covers the MTFS period and beyond.

The table below reflects the updated funding position.

Table 2

	2020/21	2021/22	2022/23	2023/24
	£m	£m	£m	£m
Revenue Support Grant	33.430	33.430	33.430	33.430
Business Rates	200.552	200.946	203.181	205.451
Council Tax	519.636	538.986	559.057	579.875
New Homes Bonus	3.503	2.405	1.635	0.799
Better Care Fund	45.532	45.532	45.532	45.532
Social Care Grant	33.417	33.417	33.417	33.417
Collection Fund Surplus	6.573	3.750	3.750	3.750
Total	842.643	858.466	880.002	902.254
Funding assumed - previous MTFS	842.190	868.476	889.200	910.059
Variance	0.453	-10.010	-9.198	-7.805

2.1 Council tax and business rates

Council tax

The MTFS currently reflects the following assumptions in relation to the county council's council tax increases as previously reported to cabinet, however this is a decision for full council to make each year when setting the budget.

Table 3

	Council tax increase (no referendum required)	Adult social care precept	Total council tax increase
2020/21	1.99%	2.00%	3.99%
2021/22	1.99%	0.00%	1.99%
2022/23	1.99%	0.00%	1.99%
2023/24	1.99%	0.00%	1.99%

Following the provisional settlement there is an option available to authorities to raise an adult social care precept of 2% for 2020/21 only. From 2021/22 onwards, it is assumed the maximum increase that we will be able to apply to council tax, without a referendum, will be 1.99%. Any decisions not to increase council tax in line with the

assumptions above would increase the financial gap; every 1% in council tax yields circa £5.000m.

Within the current MTFS a tax base increase of 1.17% is included for 2020/21 reverting to 1.7% thereafter based on historical average increases. The tax base figures for 2020/21 have been confirmed by the 12 Lancashire districts. The lower than forecast increase in taxbase results in a loss of c£3m in each year of the financial strategy. The shortfall in council tax revenue is currently offset in 2020/21 by an increase in collection fund indicated in latest figures provided by the districts. Final figures for the collection fund will be included in the budget papers for Full Council.

At this stage the average increase of 1.7% has been maintained within the MTFS for future years, as we anticipate this lower than forecast increase to be short-lived. We also expect that there will be an offsetting increase on the collection fund that could be increased due to prudent estimations of growth from district councils, based again on historical surplus positions.

Business rates

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 we anticipate to receive from the business rates collected in the area is less than its assessed need and therefore we receive a top up grant. We also build in a small amount of growth into the MTFS for our local share at 0.5%.

It has been confirmed that the 2019/20 75% business rates retention pilots will not continue in 2020/21. As a result we have sought guidance from sector experts and have remodelled our forecast based on their guidance for a 50% scheme for 2020/21, then a 75% scheme for the remainder of the forecast period. The reduction from 2021/22 onwards is largely due to elements of business rates funding, that were previously built in to the strategy across four years, confirmed as not continuing past 2020/21.

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

The salary pay pressure has been amended to reflect a change in the cost of pension contributions at an additional £3.6m. This has been offset by a future saving for a future pension prepayment and the effects of the latest triennial valuation the effects of which have led to a significantly improved position than anticipated in the previous MTFS.

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

Table 4

	2020/21 £m	2021/22 £m	2022/23 £m	2023/24 £m	Total £m
Employee costs	15.941	7.683	7.153	7.594	38.371
Pensions costs	-11.811	0.374	0.374	0.374	-10.689
Other pay related costs	0.068	0.051	0.052	0.050	0.221
Revised pay and pension requirements	4.198	8.108	7.579	8.018	27.903
Pay and pensions - previous MTFS	5.393	7.886	7.621	7.633	28.533
Variance	-1.195	0.222	-0.042	0.385	-0.630

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. The most significant adjustment in this area is as a result of the impact of the revised national living wage on the cost of commissioned services on adult social care. Following the announcement in December of the national living wage increase of 6.21% we have updated our cost assumptions for 2020/21. Our base assumption is for annual increases of 3.06% and for subsequent years we have reverted to this assumption. We will need to monitor developments in the light of government's commitment that the national living wage rate will be £10.50 by the end of current parliament should economic conditions permit. In future years, each additional 1% increase in the rate will lead to an increase in costs of c£2.200m

Table 5

	2020/21 £m	2021/22 £m	2022/23 £m	2023/24 £m	Total £m
Adults Services	19.229	12.380	13.147	15.435	60.191
Children's Services	1.704	1.545	1.420	1.990	6.659
Waste Services	2.378	2.090	2.392	2.488	9.348
Transport Services	1.397	1.463	1.553	1.632	6.045
Other Services	2.276	-1.603	1.544	2.253	4.470
Revised price inflation requirements	26.984	15.875	20.056	23.798	86.713

Price inflation – previous MTFS	24.880	16.091	20.265	23.855	85.091
Variance	2.104	-0.216	-0.209	-0.057	1.622

3.3 Demand pressures

All services have reviewed the demand pressures they face in future years and increasing demand still remains a significant element of the funding gap.

Table 6

	2020/21	2021/22	2022/23	2023/24	Total
	£m	£m	£m	£m	£m
Adults Services	17.764	10.573	10.163	8.816	47.316
Children's Services	4.226	1.827	1.190	1.737	8.980
Waste Services	-1.576	0.240	0.126	0.131	-1.079
Transport Services	2.013	0.907	0.606	0.69	4.216
Other Services	2.327	0.751	0.491	0.219	3.788
Revised Demand Requirements	24.754	14.298	12.576	11.593	63.221
Demand – previous MTFS	26.628	15.297	13.141	12.510	67.576
Variance	-1.874	-0.999	-0.565	-0.917	-4.355

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 and also taking into account future population changes, particularly with regard to the ageing population. From a social care perspective demand covers both increasing numbers of people eligible for support and the increasing complexity of those cases. The level of demand included for this service area for the four years to 2023/24 is £47.316m. This will continue to be monitored and figures may be updated in future MTFS reports.

Children's social care continues to experience demand pressures across the service, particularly in relation to placement demand due to the number of looked after children in Lancashire. The funding requirement for children's social care has increased by £8.980m over the 4 year period to reflect increased demand across children looked after placements and family support for children with disabilities. We are looking at best practice sites across the country to explore opportunities to reduce demand in a way that delivers better outcomes for children. As a result of a successful bid to the Department for Education we have commenced planning to implement Lancashire family safeguarding. The family safeguarding model is a way of keeping families together where it is safe to do so. This is achieved through a more collaborative way

of working where we motivate parents to identify the changes needed within their own families. This helps achieve better outcomes for children. This initiative is forecast to ultimately deliver c£10m of recurrent savings by 2025/26 of which £6.812m are profiled to be delivered and built into the timeframes covered by this MTFS.

A number of other initiatives are being reviewed but as yet no formal conclusions have been reached and hence no impacts are included in the MTFS.

The public and integrated transport budget continues to see rising demand pressures. As part of this MTFS an additional £4.216m has been budgeted for across 2020/21 – 2023/24.

3.4 Undeliverable savings

There is a rigorous monitoring process of agreed savings in place and throughout the year several savings have been classified as undeliverable due to changing circumstances and consultation feedback. Services are expected to find compensatory savings but in some cases it has not been possible to do this. There have been no further savings classified as undeliverable in Q3.

After the removal of all the undeliverable savings 94.5% of agreed savings are still being forecast for delivery by end of 2022/23.

3.5 Additional savings

The initial service challenge process necessarily focused on individual service reviews supported by benchmarking data which identified a number of areas where the council was high cost compared to a number of other county councils. The aim was to deliver the same or better outcomes at reduced cost wherever possible and phase 1 of the service challenge process identified £68.710m of savings proposals which were included both within the 2019/20 budget and the MTFS position. Financial benchmarking data of the cost of service position of the council relative to other county councils, reflects that some services are delivered at a relatively higher cost overall than the mean or median county council. This is largely driven by operational practice.

Phase 1 also identified a number of cross-cutting work streams and areas for investigation and review which is being taken forward as part of the service challenge phase 2 process. These work streams are more complex, requiring a fundamental challenge of, in many cases, longstanding organisational wide approaches, systems and processes to enable both service improvements and cost savings to be identified. Work is progressing on phase 2 with demand management, commissioning, organisational development, property management, commercialisation, schools traded services, transport and digital being key areas of focus. Projects on these areas and the savings options will be shared with cabinet as and when available and when timescales for their delivery are agreed. Relevant projects will be a focus for relevant finance monitoring boards as appropriate.

4. Reserves

Table 7

Reserve Name	Opening balance 2019/20	2019/20 Forecast Expenditure	Forecast Contribution to/from Reserves (Other Revenue e.g. Schools)	2019/20 forecast transfers to/from other reserves	Forecast Closing balance 2019/20	2020-21 Forecast Spend	2021-22 Forecast Spend	Forecast closing balance 31 March 2022
	£m	£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	-2.096	-1.491	0.000	0.000	-3.586	2.305	0.246	-1.036
Downsizing Reserve	-7.445	4.605	0.000	0.000	-2.840	2.840	0.000	0.000
Risk Management Reserve	-2.804	1.241	0.000	0.000	-1.562	0.763	0.800	0.000
Transitional Reserve	-164.254	16.278	0.000	-0.013	-147.989	3.086	0.244	-144.659
Service Reserves	-13.251	7.846	0.000	-2.266	-7.671	5.959	0.921	-0.791
Treasury Management Reserve	-10.000	0.000	0.000	0.000	-10.000	0.000	0.000	-10.000
SUB TOTAL - LCC RESERVES	-199.849	28.479	0.000	-2.279	-173.648	14.953	2.211	-156.485
Schools/Non-LCC Service Reserves	-17.528	1.740	0.000	0.000	-15.788	-0.018	1.790	-14.015
SUB TOTAL SCHOOLS/NON LCC RESERVES	-17.528	1.740	0.000	0.000	-15.788	-0.018	1.790	-14.015
GRAND TOTAL	-240.814	30.219	0.000	-2.279	-212.873	14.935	4.001	-193.937

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, equating to circa 3% of net budget.

The value of the uncommitted transitional reserve is currently forecast to be £147.989m by the end of March 2020. This represents a worsened position of £2.369m from the £150.250m that was previously reported to cabinet for quarter 2 in January 2020.

The transitional reserve is forecast to be sufficient to meet the identified funding gaps beyond the period of the MTFs as set out in table 8 below. Regardless, the intention remains to identify further savings to reduce the gap, and hence the call on reserves, in the future.

Table 8

	2020/21 £m	2021/22 £m	2022/23 £m	2023/24 £m
Opening Balance	147.989	148.948	147.016	131.780
Gap funding	-4.045	1.688	15.236	33.312
Commitments	3.086	0.244	0.000	0.000
Closing balance	148.948	147.016	131.780	98.468

5. Future risks and opportunities

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

5.1 Savings delivery

The scale of savings agreed to be delivered over future financial years remains significant with £64.920m currently forecast to be delivered over the period 2020/21 – 2022/23.

Any significant under-delivery or slippage to delivery timeframes will create an additional funding pressure and impact on the ongoing and longer-term financial health of the council.

There are inherent risks in the delivery of any savings programme of this scale, particularly where they are directly linked to reducing the future demand for services. However, there is a strong track record of delivery of the vast majority of previous savings plans.

However, there are comprehensive arrangements in place to track delivery of financial savings and take corrective actions where required.

5.2 Further savings opportunities

As noted in the body of the report, phase 1 of the service challenge process also identified a number of cross-cutting work streams and areas for investigation and review which are being taken forward as part of the service challenge phase 2 process. These work streams are necessarily complex, requiring a fundamental challenge of, in many cases, longstanding organisational approaches, systems and processes to enable both service improvements and cost savings to be identified. Whilst financial

benchmarking data, has identified that some services are delivered at a relatively significant higher cost overall than the mean or median county council.

Work is progressing on phase two of the service challenge process which will seek to address the ongoing deficit and is focusing on a number of cross-cutting work streams and areas for investigation and review identified in the initial phase, but where further work is needed to robustly evidence the scale and form of proposals. In particular, service challenge phase 2 is focused on the complex levers required to create an environment where service configuration and operational practice reflects best in class and supports demand management which is the single biggest driver on our costs. Cabinet members will be kept informed of the progress on each of initiatives as and when savings proposals are evaluated and timescales for their delivery are agreed.

5.3 Business rates retention / changes to funding formula

As previously explained, the future funding arrangements to be established by government pose a risk to the council. New arrangements for business rates, will not be in force before financial year 2021/22 at the earliest following a multi-year spending review and consultation during the course of 2020.

The outcome from the review may reduce funding below what is assumed in the MTFS. Conversely there is equally an opportunity that additional resources are made available through this process. The successful outcome of the Lancashire business rates pilot bid in 2019/20 has enabled the county council, districts, unitaries and fire authority to be well prepared for the implementation of the business rates retention scheme although the final details are not known at this stage.

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. The rate of growth is quite volatile, and we will continue to monitor this as part of the monthly monitoring cycle.

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, and a reducing demand increase has been built into future year's budget. The service has been looking at best practice sites across the country to explore opportunities to reduce demand in a way that delivers better outcomes for children, We will be adopting the Lancashire family safeguarding model in 2020, which will drive better outcomes for children, by focussing on early family based support, whilst also delivering an efficiency of c£10.000m per annum when the practice is fully embedded across the county.

5.5 National living wage

Given the government's commitment to raise the national living wage to £10.50 by the end of this parliament should economic conditions permit, we will need to monitor the rate at which the national living wage grows and whether there is any additional funding to support this growth. Our current assumption is that we will see net growth

of 3.06%. Should the net impact of any future increase be greater than this then there will be an increased pressure in the budget of c£2.200m for each additional 1%.

5.6 Troubled families funding

The county council currently receives funding towards working with troubled families. Where we have received written confirmation of troubled families funding this has been included in the MTFS. The spending review in September 2019 confirmed that funding would continue post 2019/20 however there was no confirmation of the likely sums available. It is assumed that funding levels will remain at 2019/20 levels. While we understand that alternative funding will be available for this work, at the moment there have been no details announced as to how this will arise. If the funding does cease this will result in a pressure on the budget of £2.100m. 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 to be made imminently and outcomes will be reflected in future MTFS reports.

5.6 MTFS assumptions and scenario analysis

As reported in Q2 given the uncertainty surrounding the future funding for local government we have tested a range of assumptions of funding scenarios to assess the level of risk that could result should alternative funding models be implemented. In producing this MTFS the Corporate Management Team has selected the most likely funding scenario.

The key assumptions that have been analysed and tested relate to the additional social care funding announced by the Chancellor and also the impact of changes to baseline funding (particularly the inclusion of revenue support grant). We have also tested the impact of possible flexibilities in council tax and in particular the levying of an adult social care precept.

The scenarios tested delivered a significant range of potential outcomes ranging from a gap of £85.915m to a surplus of £6.530m, with the most likely scenario and the basis for this MTFS forecasting a gap of £33.312 by 2023/24. In this scenario there would be a net call on reserves of £49.521m over the forecast period, but this would leave retained reserves to support the organisation beyond 2023/24 of £98.468m.

The scenarios presented clearly demonstrate the significant financial impact resulting from changes to the assumptions included within the MTFS. In all cases however, the council has sufficient reserves to support the gap through 2022/23 but only partway into 2023/24. The most likely scenario assumed within the MTFS shows that a structural deficit would still remain and reinforces the importance of addressing the underlying cost drivers within the council to secure financial sustainability moving forward.

In addition, the MTFS contains assumptions across services for funding growth, demand, inflation and pay levels. The table below shows the impact of an increase or decrease of 1% over these key elements of the projected budget requirement.

	Potential Full - Year Impact (£m)
Funding - Council Tax (1%)	+/- 5.223
Pay (1%)	+/- 2.758
Price Inflation (1%)	+/- 4.974
Demand (1%)	+/- 6.030

This stress testing gives confidence that the council can continue to live within its means for a number of years even in adverse circumstances. This does not however diminish or negate the need to make further savings but does demonstrate that the council continues to have sufficient resilience to deliver them in a measured and structured way.