Money Matters
Financial Outlook for the County Council
Medium Term Financial Strategy & Reserves as at 30th June 2020

Lancashire County Council

www.lancashire.gov.uk

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1. Executive summary

At Full Council in February 2020 the medium term financial strategy (MTFS) set out a forecast aggregated funding gap of £38.401m by the end of the 4 year period (2020/21 – 2023/24).

This report provides an updated position covering the financial years 2021/22 – 2023/24.

A review of assumptions, relating to both income and expenditure, has been undertaken to reflect the current information available. There is ongoing and unprecedented uncertainty in relation to future local government funding and the financial impact of the Covid-19 emergency has exacerbated the problem. Public services have been at the forefront of the emergency response, including local government. Councils have needed to introduce new services while providing additional financial support to existing service areas, such as adult social care. Local government is still in the process of understanding the short, medium and long term impact that COVID-19 will have on councils, including the impact on the wider economy and government macro-economic policy.

The government funding provided so far has focussed on alleviating immediate financial pressures created by COVID-19, with ongoing debate on what funding and support the government may provide in relation to ongoing COVID-19 financial pressures. The funding has focussed on COVID-19 related expenditure, and arguably has had less focus on the indirect consequences of the pandemic, in particular lost income and the ability to deliver planned savings. Further work will be required to understand the latent financial impacts on local government and this will be a matter reserved for the Spending Review.

The updated aggregated funding gap contained within the report is £79.306m by 2023/24 which is an increase of £40.905m from the previously reported position in February. The forecast includes our latest estimate of the funding and cost implications of the pandemic including collection fund impacts, which were also reported in the Covid-19 financial update report to Cabinet in August, along with other non-Covid related adjustments. The main reasons for the changes to the position are as follows:

- The current forecast collection fund deficit of £30m for 2020/21 which after the Local Government Secretary announcement on the 2nd July of a proposal for a phased repayment of council tax and business rates deficits over 3 years, leading to an in year pressure of £10m for each of years 2021/22-2023/24.
- Removal of the historic collection fund surplus forecast of £3.750m per annum.
- An assumed zero tax base increase for 2021/22 as a result of Covid related disruption to housing development with consequent decrease in funding available of £9.010m. With pre-Covid growth of 1.7% per annum assumed thereafter.
- The reflection of the latest Office for Budget Responsibility forecast for the increase in National Living Wage which has an impact on the cost of provision of commissioned adult social care.

- Following a review of current activity, updated demand and volume assumptions in line with ONS population statistics.
- The pay award for 2020/21 likely to be agreed at higher than the 2% budgeted level.

The overall position over the 3 year period indicates a structural deficit of £52.209m in 2021/22 rising to an aggregated deficit of £79.306m by 2023/24, assuming no additional government financial support in those years.

The outcome of the Spending Review which will be published in the autumn will be fundamental to the future financial position of the council. To address the forecast pressure officers, working with our national organisations, particularly in adults and children's services which are the most significant areas of financial pressure due to the increasing demand and cost of services going forward, will develop an evidence base and narrative to influence the forthcoming Comprehensive Spending Review for which submissions will be accepted up until 24th September 2020.

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 the changes to be made in respect of business rates retention, and the overall funding formula which have been delayed for a further year, the anticipated green paper on adult social care and the aforementioned government spending review being significant for our future funding stream.

The value of the uncommitted transitional reserve is currently forecast to be sufficient to meet the identified funding gaps for the first two years of the MTFS, which provides time to address the structural deficit in a considered and sustainable way. We will look to maximise efficiencies across services and commence work to identify potential savings should a poor settlement arise.

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

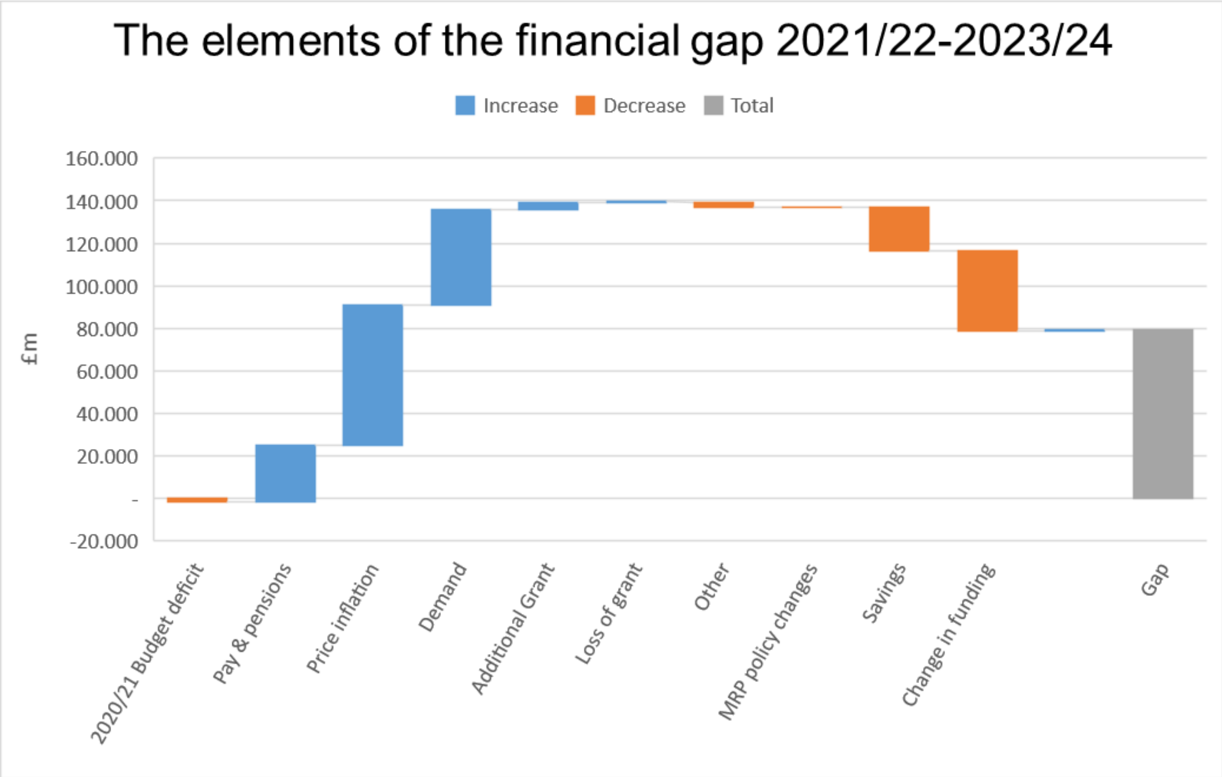
Table 1

	2021/22 £m	**2022/23 £m**	**2023/24 £m**	**Total £m**
Spending Gap as reported to Full Council February 2020	**6.763**	**13.563**	**18.076**	**38.401**
Add change to forecast of spending:				
Pay & Pensions	2.636	0.005	0.076	**2.717**
Inflation and Cost Changes	5.332	1.452	-0.381	**6.403**

Service Demand and Volume Pressures	2.402	1.080	2.820	**6.302**
Other	3.831	0.000	0.000	**3.831**
Undeliverable Savings	1.409	0.000	0.000	**1.409**
Covid Impact/Pressures	6.702	-3.067	-3.302	**0.333**
Total Change to Forecast of Spending	**22.312**	**-0.530**	**-0.787**	**20.995**
Change to forecast of resources:				
Funding	23.134	-1.977	-1.247	**19.910**
Total Change to Forecast of Resources	**23.134**	**-1.977**	**-1.247**	**19.910**
Funding Gap	**52.209**	**11.055**	**16.042**	**79.306**
Forecast net budget requirement	887.554	869.913	898.400	
Funding	835.345	858.858	882.358	

Aggregated Funding Gap	**2021/22**	**2022/23**	**2023/24**
2021/22 (£m)	52.209	52.209	52.209
2022/23 (£m)		11.055	11.055
2023/24 (£m)			16.042
2024/25 (£m)			
Total	**52.209**	**63.264**	**79.306**
Previous position (£m)	**6.763**	**20.325**	**38.401**
Variance (£m)	**45.446**	**42.939**	**40.905**

The graph below demonstrates the drivers that make up the changes in the financial surplus of £1.358m carried forward from 2020/21 to the cumulative position of £79.306m in the financial year 2023/24 shown in the table above:



2. Funding

The Chancellor launched the 2020 Comprehensive Spending Review in July 2020. This is due to be published in the autumn and will set out the Government's revenue spending plans for 2021-22 to 2023-24.

The Chancellor has not set a 'spending envelope' because of the uncertainty caused by COVID19, and has asked Departments to identify opportunities to reprioritise and deliver savings, however he did confirm that departmental spending will grow in real terms across the CSR period.

Business Rates

A review of business rates was previously announced in the spring 2020 Budget. The effect of COVID19 on the economy, has made fundamental change to business rates, which could even see them being replaced with a different business tax, much more likely.

The next business rates revaluation was due to take effect on 1 April 2022 (based on a valuation date of 1 April 2019). A postponement of revaluation was announced in May 2020. The Chancellor's statement confirmed that the next revaluation will take place on 1 April 2023, and will be based on property values as of 1 April 2021 in order to better reflect the impact of COVID19.

Fair Funding Formula

The fair funding formula was due to be in place by April 2021. Following the Covid pandemic, this has been delayed until at least April 2022.

Due to the financial uncertainty created by the pandemic it has been necessary to make some assumptions around the future funding envelope, the most significant being:

- From the latest returns from districts, the council's share of a collection fund deficit of £30m is forecast. In line with government guidance this is to be repaid over financial years 2021/22-2023/24.
- No increase in tax base has been forecast in 2021-22, with a return to pre-Covid levels of 1.7% per annum thereafter.
- Council tax increases of 1.99% will be applied each year.
- No growth or uplift on business rates has been built into 2021/22 with a return to growth of 0.5% per annum thereafter.
- No adult social care precept is assumed for the entirety of the forecast period
- Revenue support grant will be rolled over for the duration of this strategy.
- The social care will be rolled over for the duration of this strategy.

The table below reflects the updated funding position.

Table 2

	2021/22 £m	**2022/23 £m**	**2023/24 £m**
Revenue Support Grant	33.430	33.430	33.430
Business Rates	200.573	205.120	208.986
Council Tax	529.989	549.725	570.196
New Homes Bonus	2.405	1.635	0.799
Better Care Fund	45.532	45.532	45.532
Adult Social Care Support Grant	33.417	33.417	33.417
Collection Fund	-10.000	-10.000	-10.000
Total	**835.346**	**858.859**	**882.360**
Funding assumed - previous MTFS	858.480	880.016	902.270
Variance	-23.134	-21.157	-19.910

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
2021/22	1.99%	0.00%	1.99%
2022/23	1.99%	0.00%	1.99%
2023/24	1.99%	0.00%	1.99%
2024/25	1.99%	0.00%	1.99%

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.

For 2021-22, no tax base increase has been built in to the forecast, but returns to 1.7% increase in the years following. This has been assumed based on historical average increases.

There is no assumption of an Adult Social Care precept for the entirety of the forecast.

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 our assessed need and therefore we receive a top up grant. Previously, we have also built in a small amount of growth into the MTFS for our local share at 0.5%.

As a result of the impact of Covid 19, the business rates review has been delayed and so it is assumed that 2021/22 will effectively be a 'rollover' of 2020/21 – a continuation of the 50% scheme, with the 75% scheme forecast to be in place from 2022/23 onwards.

No growth or uplift has been forecast for 2021/22. 0.5% growth has been built in to the local share forecast from 2022/23 onwards.

Collection Fund

One of the measures announced by the Government to try and mitigate the budget pressures on local authorities as a result of collection fund deficits was that any deficit for 2020/21 will be repaid over the following three years.

The latest information received from districts suggests that there will be a c£30m pressure for LCC as a result of the collection fund issue and thus a c£10m in year pressure for financial years 2021/22-2023/24.

The funding aspects for future year's collection fund deficits are to be revealed as part of the spending review in the autumn.

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

There is an updated assumption that the pay settlement for 2020/21 will be 3%. The budget was originally set based on a 2% increase. We have therefore included the differential for 2020/21 into the 2021/22 MTFS and reverted to 2% annual increases thereafter.

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

Table 4

	2021/22 £m	2022/23 £m	2023/24 £m	Total £m
Employee costs	10.32	7.159	7.668	**25.147**
Pensions costs	0.374	0.374	0.374	**1.122**
Other pay related costs	0.05	0.051	0.052	**0.153**
Revised pay and pension requirements	**10.744**	**7.584**	**8.094**	**26.422**
Pay and pensions - previous MTFS	**8.108**	**7.579**	**8.018**	**23.705**
Variance	2.636	0.005	0.076	2.717

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 last December of the national living wage increase (NLW) of 6.21% we updated our cost assumptions for 2020/21 and have incorporated the latest of 5.5% increase for 2021/22 but reverted to a base assumption for annual increases of 3% for subsequent years. Given the latest Office for Budget Responsibility projections we have updated our forecasts to follow the predicted increases. 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. Each additional 1% increase in the rate will lead to an increase in costs of c£1.600m per annum.

The updated inflationary pressures are analysed across the authority as per table 5:

Table 5

	2021/22 £m	2022/23 £m	2023/24 £m	Total £m
Adults Services	17.673	13.911	14.705	**46.289**
Children's Services	1.394	1.923	2.163	**5.480**
Waste Services	2.124	2.361	2.479	**6.964**
Transport Services	1.463	1.553	1.632	**4.648**
Other Services	-1.447	1.760	2.438	**2.751**
Revised price inflation requirements	**21.207**	**21.508**	**23.417**	**66.132**
Price inflation – previous MTFS	**15.875**	**20.056**	**23.798**	**59.729**
Variance	**5.332**	**1.452**	**-0.381**	**6.403**

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

	2021/22 £m	2022/23 £m	2023/24 £m	Total £m
Adults Services	10.014	9.079	9.540	**28.633**
Children's Services	4.135	3.263	3.859	**11.257**
Waste Services	0.734	0.202	0.212	**1.148**
Transport Services	0.907	0.606	0.690	**2.203**
Other Services	0.910	0.506	0.112	**1.528**
Revised Demand Requirements	**16.700**	**13.656**	**14.413**	**44.769**
Demand – previous MTFS	**14.298**	**12.576**	**11.593**	**38.467**
Variance	**2.402**	**1.080**	**2.820**	**6.302**

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 three years to 2023/24 is £28.633m. 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 £11.257m over the 3 year period to reflect increased demand across children looked after placements and family support for children with disabilities. We are working towards the implementation of the 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£12m of recurrent savings by 2023/24.

3.4 Other cost pressures

There are further costs of £3.831m which have been reviewed and assessed as recurrent pressures to the budget the most significant being:

1. The rollout of Microsoft Office 365 across the council will deliver greater efficiencies and improved collaboration for all colleagues across the authority. The ongoing revenue cost of the software is £1.438m.

2. Following a review of the outturn position of a number of revenue budgets it is apparent that there is a recurrent pressure of £2.356 as a result of under delivery of income. We have reviewed the service budgets and have been unable to identify mitigating underspends elsewhere. The pressure has arisen over a number of years and services have made every attempt to improve the position. The most significant sums are in relation to school catering £1.340m and design and construction £575,000.

3.5 Undeliverable savings

There is a rigorous monitoring process of agreed savings in place. Three savings have been classified as undeliverable in Q1 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. These savings relate to Lancashire Break Time (£765,000), the Lancashire Youth Offending team, for which there was no pan Lancashire desire for a consolidated team (£500,000 and a loss of income surrounding the closure of Whitehough (£144,000). After the removal of these undeliverable savings 93.8% of agreed savings are still being forecast for delivery by end of 2022/23.

4. Reserves

Table 7

Reserve Name	Opening balance 2020/21	2020/21 Forecast Expenditure	2020/21 Forecast transfers to/from other reserves	2020/21 Forecast Closing Balance	2021-22 Forecast Spend	2022-23 Forecast Spend	Forecast closing balance 31 March 2023
	£m	£m	£m	£m	£m	£m	£m
County Fund	-23.437	0.000	0.000	-23.437	0.000	0.000	-23.437
SUB TOTAL - COUNTY FUND	**-23.437**	**0.000**	**0.000**	**-23.437**	**0.000**	**0.000**	**-23.437**
Strategic Investment Reserve	-5.819	0.163	0.000	-5.656	3.140	0.695	-1.821
COVID-19 Reserve	-33.961	33.961	0.000	0.000	0.000	0.000	0.000
Downsizing Reserve	-5.642	2.840	0.000	-2.802	2.802	0.000	0.000
Risk Management Reserve	-1.935	0.916	0.000	-1.018	0.914	0.104	0.000
Transitional Reserve	-151.199	1.250	-0.346	-150.295	0.494	0.069	-149.731
Service Reserves	-16.633	12.124	0.000	-4.509	1.928	0.746	-1.835
Treasury Management Reserve	-11.597	0.000	0.000	-11.597	0.000	0.000	-11.597
SUB TOTAL - LCC RESERVES	**-226.785**	**51.254**	**-0.346**	**-175.877**	**9.278**	**1.615**	**-164.984**
Schools/Non-LCC Service Reserves	-17.873	1.034	0.346	-16.493	2.023	-0.144	-14.613
SUB TOTAL SCHOOLS/NON LCC RESERVES	**-17.873**	**1.034**	**0.346**	**-16.493**	**2.023**	**-0.144**	**-14.613**
GRAND TOTAL	**-268.095**	**52.288**	**0.000**	**-215.807**	**11.301**	**1.471**	**-203.035**

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 £150.295m by the end of March 2021. This represents an improved position of £4.034m from the £146.261m that was previously reported to cabinet in February 2020.

The transitional reserve is forecast to be sufficient to meet the identified funding gaps for financial years 2021/22, 2022/23 and partway through 2023/24as set out in table 8 below.

Table 8

	2021/22	2022/23	2023/24
Opening Balance	150.295	97.593	34.260
Gap funding	52.208	63.263	79.305
Commitments	0.494	0.069	0.000
Closing balance	**97.593**	**34.260**	**-45.044**

5. Future risks and opportunities

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

5.1 The financial impacts of the ongoing Covid-19 response
The longer term financial impacts of the response to the pandemic remain unclear. A protracted recovery period or a subsequent spike are likely to lead to further financial pressures to the authority.

The ongoing impacts and revision to service delivery and to service user demand for service and the way it is delivered post pandemic could lead to volatility of pressure on the budget.

We are assessing the ongoing need for additional and ceased services in response to the situation and will evaluate the revised budget requirement as a result.

The spending review in the autumn will hopefully address the known future pressures and we will update our MTFS as the outcome of the review and subsequent local government settlement becomes clear.

For the purposes of this MTFS we have assumed that there are no additional impacts in relation to the virus beyond the current financial year.

5.2 Savings delivery
The scale of savings agreed to be delivered over future financial years remains significant with £25.568m currently forecast to be delayed in 2020/21 as a result of refocussing officer priorities to the response to the current pandemic. In addition there are forecast savings of £13.430m to be delivered over financial years 2021/22 – 2022/23.

Should the Covid emergency response continue for or protracted period or re-emerge as a result of a second spike it is likely that there will be further slippage.

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

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 2022/23 at the earliest following a multi-year spending review and consultation during the course of 2021.

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.

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 are working on adopting the Lancashire family safeguarding model in the current financial year, which will drive better outcomes for children, by focussing on early family based support, whilst also forecasting the delivery a saving of c£12m per annum when the practice is fully embedded across the county.

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

	Potential Full - Year Impact (£m)
Funding - Council Tax (1%)	+/- 5.299
Pay (1%)	+/- 2.637
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 the next two years 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.