AGENDA ITEM:

REPORT TO:	**MERSEYSIDE FIRE & RESCUE AUTHORITY BUDGET MEETING**
DATE:	**18TH FEBRUARY 2010**
REPORT NO.	**CFO/013/10**
REPORTING OFFICER:	**EXECUTIVE DIRECTOR OF RESOURCES**
CONTACT OFFICER:	**MR. KIERAN TIMMINS, EXTN. 4202**
OFFICERS CONSULTED:	**EXECUTIVE LEADERSHIP TEAM**
SUBJECT:	**MERSEYSIDE FIRE AND RESCUE AUTHORITY BUDGET AND FINANCIAL PLAN 2010/2011 –2014/2015**

Merseyside Fire and Rescue Authority Budget and Financial Plan 2010/2011- 2014/2015

APPENDIX	**1**	**TITLE:**	**FIRE SERVICE BASE BUDGET 2010/11**
APPENDIX	**2A**	**TITLE:**	**AUTHORITY APPROVED CAPITAL PROGRAMME FOR 2010/2011 – 2013/14**
APPENDIX	**2B**	**TITLE:**	**2010-2015 NEW START CAPITAL BIDS**
APPENDIX	**3**	**TITLE:**	**TREASURY MANAGEMENT CLAUSES TO FORM PART OF STANDING ORDERS AND FINANCIAL REGULATIONS**
APPENDIX	**4**	**TITLE:**	**WEIGHTED SCORECARD OF BUDGET OPTIONS**

ATTACHED – ELECTRONIC / HARD COPY

Beacon Authority 2004-2005 Services for Older People

Beacon Authority 2006-2007 Early Intervention (Children at Risk)

Beacon Authority 2008-2009 Reducing Health Inequalities

Purpose of Report

1. To present information to allow Members to set a medium term financial plan – both capital and revenue – that allocates resources in line with the Authority's strategic aims and ensures that the Authority delivers an efficient, Value for Money service. This will also allow the Authority to determine a budget for 2010/2011 and a precept level in line with statutory requirements.

Recommendation

2. Members consider this report and:-

   (a) Confirm their strategy on balances and the level of balances and reserves they consider appropriate for the forthcoming and future financial years.

   (b) Decide the level of precept they wish to set for 2010/2011 and any strategy for precepts they wish to adopt for future years.

   (c) Choose the growth and savings options they wish to support to deliver a balanced Medium Term Financial Plan.

   (d) Confirm the capital strategy and investment strategy they wish to adopt for 2010/2011 and future years.

   (e) Note the prudential indicators relating to the proposed capital programme and agree the Treasury Management indicators set out in the Treasury Management Strategy for:-

      (i) External Debt
      (ii) Operational Boundary for Debt
      (iii) Upper limits on fixed interest rate exposure
      (iv) Upper limits on variable rate exposure
      (v) Limits on the maturity structure of debt
      (vi) Limits on investments for more than 364 days

   (f) Noting that these policies and parameters provide an approved framework within which the Officers undertake the day to day capital and treasury activities (the Authority is recommended to approve each of the key elements contained within this section of the report), and

   (g) Amend the Authority's Standing Orders and Financial Regulations as outlined in Appendix 3 to reflect latest CIPFA guidance.

   (h) Nominate the Performance & Audit Committee to have responsibility for the effective scrutiny of the treasury management strategy and policies.

   (i) Approve the statement within this report that sets out the Authority's policy on the Minimum Revenue Payment (MRP) for 2010/11.

Information & Background

3. The Authority is required to determine its budget and precept level for 2010/2011 by 1st March 2010.

4. This report will present all the necessary financial information in a single report. This report considers:-

Forecast Revenue Estimates
The Proposed Capital Programme
Savings and Growth Options
The Treasury Management Strategy
The Minimum Revenue Payment policy for the Authority

5. Considering all the financial issues to be taken into account in a single report ensures that the Authority can:-

(a) consider the borrowing freedoms available under the prudential code
(b) reflect best practice
(c) provide value for money
(d) focus on the link between capital investment decisions and revenue budgets
(e) continue developing their strategic financial planning

6. The following report structure will be adopted:-

Section	**Focus**
A	Executive Summary
B	Background Information
C	Five Year Capital Programme
D	Minimum Revenue Provision Statement
E	Prudential Indicators
F	Treasury Management Strategy
G	Revenue Forecasts 2010/2011 – 2014/2015
H	Options for Delivering a Balanced Plan
I	Adequacy of Reserves and Balances

(A) EXECUTIVE SUMMARY

The Authority must set a balanced budget and a precept level by 1st March 2010.

The budget and financial plan should allocate resources in line with corporate priorities. The key aims of Merseyside Fire and Rescue Authority are set out in its Integrated Risk Management Plan and may be summarised as:

Our Vision – "Making Merseyside a safer, stronger, healthier community"

Our Mission – "To work in partnership to provide an excellent, affordable service that will:

Reduce risk throughout the community by protective community safety services

Respond quickly to emergencies with skilful staff

Restore and maintain quality of life in our communities

The Authority has agreed a number of Value For Money Principles that have underpinned its approach to budgets and financial plans in recent years. They are:-

Principle 1 – Allocate resources In line with priorities
Principle 2 – Control Council Tax
Principle 3 – Acknowledging budget realities

The Authority will continue to:

(i) ***Acknowledge the challenges it faces;***
(ii) ***Acknowledge the reality of its budget and recognise that 80% of its costs are people related.***

Principle 4 – The Authority seeks to avoid compulsory redundancy in delivering VfM

Principle 5 - The Authority seeks to maintain or improve service levels to make Merseyside safer, stronger, healthier

Revenue Forecasts

7. A five-year financial revenue estimate has been prepared based upon the current strong medium term financial plan agreed last year by all parties. Whilst there are some minor changes broadly the plan remains robust. This is set out below. The revenue position is considered in more detail in section G.

2010/11 - 2014/15 APPROVED FINANCIAL PLAN	2010/11	2011/12	2012/13	2013/14	2014/15
	£'000	£'000	£'000	£'000	£'000
Approved Base Expenditure	73,767	76,055	77,926	79,754	82,019
Planned (Use) / Contribution to Cost Smoothing Reserve	-125	-392	-182	137	85
Approved 2009/10 5 Year Budget Financial Plan	73,642	75,663	77,744	79,891	82,104
Approved Amendments & Technical adjustments:					
Impact of lower 2009/10 pay awards	-450	-450	-450	-450	-450
Directors growth	143	145	145	145	145
Committee Approved Changes	0	53	53	15	15
Anticipated impact on Investment Income due to lower interest rates	0	50	0	0	0
Increase in NI rates by a further +0.5% from 2011/12 PBR		250	250	250	250
Ajustment to Planned (Use) / Contribution to Cost Smoothing Reserve	-9	-143	-96	-63	-67
Updated MTFP for 2010/11 Budget Report	73,326	75,568	77,646	79,788	81,997
Forecast Income					
Government Grant increase, +0.5% in 2010/11 then +2% thereafter	-46,304	-47,230	-48,175	-49,139	-50,122
Council Tax Increase assumed 4%	-27,336	-28,429	-29,566	-30,749	-31,979
Reduction in Council Tax Base	49	51	53	55	57
Collection fund deficit	226	0	0	0	0
Forecast Income in Financial Plan	-73,365	-75,608	-77,688	-79,833	-82,044
Forecast position (surplus) / deficit	-39	-40	-42	-45	-47

8. This forecast identifies a small surplus for 2010/11 – 2014/15, subject to a 4% increase in the 2010/11 precept and each year thereafter, and the achievement of the efficiency savings approved in 2009/10. In 2009/10 the Authority approved a set of options to deliver approximately £5.0m of savings over the 2009/10 – 2014/15 period as set out below:

Description	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
	£'000	£'000	£'000	£'000	£'000	£'000
Saving Options:						
Effectively Reducing ill health retirements	-200	-350	-350	-350	-350	-350
Review management Structures	-400	-400	-400	-400	-400	-400
Non Uniform Support Costs	-150	-150	-150	-150	-150	-150
Special Appliance provision/ORC	-280	-280	-280	-280	-280	-280
Grey Book/Green Book Review	-250	-250	-250	-250	-250	-250
Further Review of RRT (11 posts)	-400	-400	-400	-400	-400	-400
LLAR * 1	-300	-300	-300	-300	-300	-300
Apply Retirement Rengagement	0	-175	-175	-175	-175	-175
Income Generation through social enterprise	0	-175	-200	-225	-250	-250
Procurement Efficiencies Target	-200	-250	-250	-250	-250	-250
Self Rostering	-360	-360	-360	-360	-360	-360
Reduce R&R team to reflect riding appliances efficiently in line with agreements	-1,332	-1,332	-1,332	-1,332	-1,332	-1,332
Engineering Centre of Excellence	0	-150	-150	-150	-150	-150
Use of Cost Smoothing Reserve	283	-125	-392	-182	137	85
	-3,589	-4,697	-4,989	-4,804	-4,510	-4,562

9. This medium term financial plan assumes that all the approved saving options can and will deliver the required forecast savings. Other factors that have now been built into the updated financial plan include:-

- The impact of lower than expected pay awards in 2009/10
- The increase in Employers National Insurance contributions
- Interest rates affecting investment income
- Directors growth requests
- Approved budget amendments ratified by the Authority throughout 2009/10
- Reduction in the Council Tax base

10. Key assumptions in this base forecast include:-

- Provision for no pay increase for all staff in 2010/11 & 2011/12, then 2% p.a. thereafter.
- Any future increases in employer costs such as pension contributions can be contained within the overall pay bill increase of 2% p.a.
- Provision for grant increases of 0.5% in 2010/11, and then 2% from 2011/12 onwards.
- Assumption that the Authority will have the freedom to set council tax levels at 4%

11. As significant risk exists around the key assumptions in the plan and potential variations can substantially impact on the medium term financial plan, **for planning purposes only**, the service has adopted an efficiency target of £8m by 2015 over and above the approved efficiencies in the current financial plan. Officers will work with the Budget Working Group to identify the options to deliver further efficiencies

Reserves and Balances

12. In the light of the financial risks facing the Authority the Executive Director of Resources recommends that the Authority should aim to, in the medium term, maintain the following reserves as part of its financial plans

	31.03.10	31.03.11	31.03.12	31.03.13	31.03.14	31.03.15
	£'000	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
SPATE / Other Emergencies						
Bellwin Reserve	**147**	147	147	147	147	147
Insurance Reserve	**220**	220	220	220	220	220
Emergency planning	**75**	75	75	75	75	75
Modernisation Challenge						
FB Modernisation Reserve	**581**	581	581	581	581	581
Smoothing Reserve	**2,391**	2,257	1,722	1,444	1,518	1,536
Capital Investment						
PFI/Capital Reserve	**695**	695	695	695	695	695
Specific Projects						
Job Evaluation Reserve	**430**					
Regional Reserve	**100**	100	100	100	100	100
Training Reserve	**195**	195	195	195	195	195
Inflation						
Inflation Reserve	**858**	858	858	858	858	858
Total Earmarked Reserves	**5,692**	5,128	4,593	4,315	4,389	4,407
General revenue Reserve	**2,543**	2,543	2,543	2,543	2,543	2,543
Total reserves	**8,235**	**7,671**	**7,136**	**6,858**	**6,932**	**6,950**

13. As previously stated this report identifies a number of potential risks in relation to the key assumptions in the medium term financial plan. If any of these assumptions vary then the forecast balanced budget position will be affected. Any resultant material deficit might result in the Authority having difficulty in maintaining its value for money principles and in particular avoiding compulsory redundancies. In order to maximise the flexibility to manage these risks and to stick to its value for money principles the Authority should consider seeking opportunities to maximise reserves over the next three years. If any such short term reserves are then not required they may be prudently reinvested in making Merseyside safer, stronger and healthier.

14. **Members should bear in mind that reserves and balances and one-off savings should only be used to finance one-off expenditure. If such monies are used to fund ongoing revenue expenditure without taking action to reduce underlying expenditure, the Authority would find itself facing the same deficit in the next and future years but without reserves available to finance it. This is underlined by the District Auditor's 'Golden Rule' - that "one off" revenue reserves should not be used to support 'ongoing' revenue expenditure.**

Council Tax Increase

15. The forecast produced assumes a 4.00% council tax increase in each year in line with the Authority value for money principles. The Authority may choose to use a further precept increase to bridge the gap. However central government has made it clear that large increases will not be tolerated:-

"*As I said in my statement to the House of Commons, I am pleased that the average Band D council tax increase this year was 3 per cent. The Government anticipates this amount to fall further in 2010/11….we expect the average Band D tax increase on England to achieve a 16 year low in 2010/11. The Government remains prepared to take capping action against excessive increases by authorities*…" (Barbara Follett MP, Parliamentary Under-Secretary of State for Communities and Local Government, letter to Local Authority Leaders 09.12.09)

Government has used its powers in recent years and capped a number of authorities.

16. The ready reckoners below show the impact of potential Council Tax increases:

Council Tax Increase

	0%	1%	3.85%	4%	5%
Band D Tax	62.37	62.99	64.77	64.86	65.49
District Precept	£m	£m	£m	£m	£m
LIVERPOOL	7.819	7.896	8.120	8.131	8.210
WIRRAL	6.530	6.594	6.781	6.790	6.856
ST.HELENS	3.474	3.509	3.608	3.613	3.648
SEFTON	5.804	5.861	6.027	6.035	6.094
KNOWSLEY	2.611	2.637	2.711	2.715	2.742
	26.238	26.497	27.247	27.284	27.550

Members must choose a portfolio of savings and growth options, a strategy for reserves (in the light of the advice of the Executive Director of Resources) and a Council Tax level for 2010/2011 that sets a balanced budget in line with the statutory timetable.

Capital

17. The proposed 5-year capital programme is detailed in section C.

18. The table below summarises the proposed investments which are mainly in the Authority's property, vehicle and ICT assets which total nearly £37 million across the life of the programme.

2010 - 2015 Proposed Capital Investment

Type of Expenditure	Total Cost £	2010/11 £	2011/12 £	2012/13 £	2013/14 £	2014/15 £
Building/Land	**8,868,000**	5,745,500	816,000	1,005,500	306,000	995,000
Hydrants	**185,000**	37,000	37,000	37,000	37,000	37,000
Fire Safety	**8,762,000**	1,752,000	1,752,000	1,752,000	1,752,000	1,754,000
ICT	**2,170,000**	603,000	373,000	328,000	333,000	533,000
RCC - ICT investment	**70,000**	50,000	20,000	0	0	0
Operational Equipment	**951,700**	676,700	20,000	195,000	20,000	40,000
T.D.A.	**110,000**	110,000	0	0	0	0
Vehicles	**8,622,600**	2,978,400	1,553,600	1,008,600	1,672,800	1,409,200
Fire World	**7,035,000**	0	0	3,560,000	3,475,000	0
TOTAL	**36,774,300**	**11,952,600**	**4,571,600**	**7,886,100**	**7,595,800**	**4,768,200**
Financing Available:	**Total £**	**2010/11 £**	**2011/12 £**	**2012/13 £**	**2013/14 £**	**2014/15 £**
Capital Receipts	900,000	900,000	0	0	0	0
External Contributions	6,035,000	0	0	3,060,000	2,975,000	0
R.C.C.O.	5,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Grant	1,072,000	1,072,000	0	0	0	0
	13,007,000	2,972,000	1,000,000	4,060,000	3,975,000	1,000,000
Borrowing Requirement						
supported	16,899,347	3,251,000	3,316,020	3,382,340	3,449,987	3,500,000
unsupported	6,867,953	5,729,600	255,580	443,760	170,813	268,200
Borrowing	23,767,300	8,980,600	3,571,600	3,826,100	3,620,800	3,768,200
Total Funding	36,774,300	11,952,600	4,571,600	7,886,100	7,595,800	4,768,200

19. This capital programme has a borrowing requirement of £8.981million in 2010/2011 and nearly £24m across the whole life of the plan.

20. The proposed programme does contain significant prudential borrowing. The total of unsupported/prudential borrowing is £6.868million across the life of the programme. This is the amount of borrowing above what Government assumes in grant calculations.

The Authority needs to be mindful of the revenue costs of such borrowing.

21. Whilst there has been a relatively large increase in authority debt levels in recent years, debt servicing costs will still make up a relatively small portion of the Authority's overall costs. This is considered affordable, prudent and sustainable in the light of the prudential indicators calculated for the Authority as long as such a decision is combined with action to tackle the underlying budgetary deficit (Section E)

Treasury Management

22. The Prudential Code requires the Authority to set a Treasury Management Strategy that includes number of indicators and limits. It sets a framework for the Executive Director of Resources to manage investments and borrowings within.

23. The proposed strategy is set out in section F and includes limits for the next three years on:-

Overall Level of External Debt
Operational Boundary for Debt
Upper limits on fixed interest rate exposure
Upper limits on variable rate exposure
Limits on the maturity structure of debt
Limits on investments for more than 364 days

Minimum Revenue Payment (MRP) Statement

24. MRP is the amount of money set aside in the revenue budget by the Authority each year to reduce its overall level of debt. The Authority is required under the new Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 to prepare a statement on its policy for MRP in respect of the forthcoming year. The new regulations require authorities to pay debt at a rate which it considers prudent.

25. The Executive Director of Resources has reviewed the MRP policy in line with the legislation and the report outlines the proposed MRP policy for 2010/11 and future years.

26. The overall impact of the new regulations has been to increase the revenue costs relating to asset investment.

(B) BACKGROUND INFORMATION

27. This section provides general financial information on the Authority's finances and financial health.

Corporate Strategy

28. If any organisation wants to be successful its budget setting and medium term financial plan needs to reflect the allocation of resources to support the key strategic aims and priorities.

29. For the many years now the Authority has maintained a comprehensive five year financial plan and capital programme. This report will build upon this strategic approach to financial matters. The Authority recognises significant uncertainty exists over some of the key assumptions within the plan in the medium term, particularly around the level of government grant support beyond 2010/11 as it seems likely that government support will be reduced in future years.

30. Members will recognise that this report is prepared at a time when the fire service faces a period of tremendous change and challenge. A number of key issues will need to be addressed as part of any financial strategy and in particular cater for the ongoing modernisation of the fire service and the Integrated Risk Management Plan (IRMP).

31. The Integrated Risk Management Plan (IRMP) is the key driver in the allocation of the Authority's resources in response to the risks facing Merseyside.

32. The Authority's IRMP states the main strategic themes that the Authority has been progressing and its plans for the future, detailing the ways in which the Authority has been at the forefront of driving forward the modernising agenda for the fire service for a number of years now. The third draft IRMP was approved by the Authority for the period 2010/11 and the final version will be presented to the Authority on 18th March 2010 alongside the Service Plan, which will contain the IRMP action points for that year. Although it remains a three year plan, the current IRMP will be refreshed annually to ensure that it maintains currency.

33. The Authority's key visions and aims as set out in the IRMP are set out below. Any financial plan should aim to allocate resources to deliver these key aims:

"Our Vision – "Making Merseyside a safer, stronger healthier community"

Our Mission – "To work in partnership to provide an excellent, affordable service that will:

Reduce risk throughout the community by protective community safety services

Respond quickly to emergencies with skilful staff

Restore and maintain quality of life in our communities

These are not new aims for Merseyside. The Authority has moved well in advance of central direction and has had a very similar strategy for several years now based upon focussing resources on community fire safety.

Is the Overall Strategy Working?

34. The Fire Authority has achieved very great success in its aims to make Merseyside a safer community. Members receive detail on this excellent performance in a variety of formats but very briefly the Authority has:-

- Become the first fire authority in the world to visit 100,000 households in a single year (and over 600,000 visits have been carried out)
- Fitted approximately 700,000 free smoke alarms
- Received Beacon Status for Early Intervention (Children at Risk), working with Older People, and for Reducing Health Inequalities
- Formed Joint Police / Fire Service Threat Response Group
- Reduced fire deaths from an average of 20 in 1999 to 9 in 2008/09 and to just 5 so far this year (year ends March), a 55% reduction.
- Employed advocates in such diverse areas as age, disability, deafness, drugs, alcohol, arson and anti-social behaviour, as well as multilingual specialists.

The table below summarises some key performance over the last 6 years:

Year	Accidental Dwelling Fires	Injuries in Accidental Dwelling Fires	Fatalities in Accidental Dwelling Fires	Anti Social Behaviour Fires
2003-2004	1612	171	9	18984
2004-2005	1470	173	11	12258
2005-2006	1456	155	11	11689
2006-2007	1336	126	8	12721
2007-2008	1286	69	9	10449
2008-2009	1302	107	9	7648
2009-2010 Q3	976	91	5	6011
Reduction between 2003/04 t0 2008/09	-19.2%	-37.4%	0.0%	-59.7%

Source: Service Plan
(Reduced fire deaths from an average of 20 in 1999 to 9 in 2008/09, a 55% reduction)

35. More details of the Authority's performance can be found in:-

- The quarterly service plan update reports, the most recent of which was CFO/262/09 (Performance & Audit Committee 19th November 2009), http://www.merseyfire.gov.uk/aspx/pages/fire_auth/pdf/Agenda_Performance_&_Audit_Mtg_191109.pdf

- The 2009/10 Service Plan can be found on the Authority's website http://www.merseyfire.gov.uk/aspx/pages/reports/pdf/08_Service_Plan_2009-10_Final_Published_01.pdf

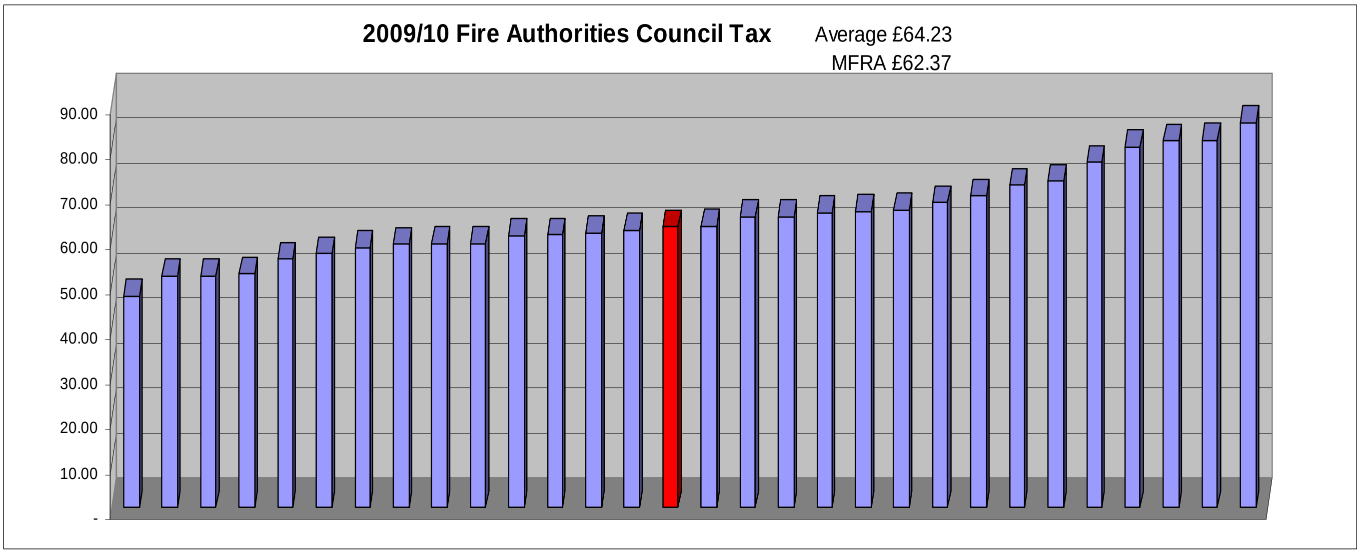
<u>Financial Strategy and where are we now?</u>

36. In recent years the Authority has adopted a financial strategy that:

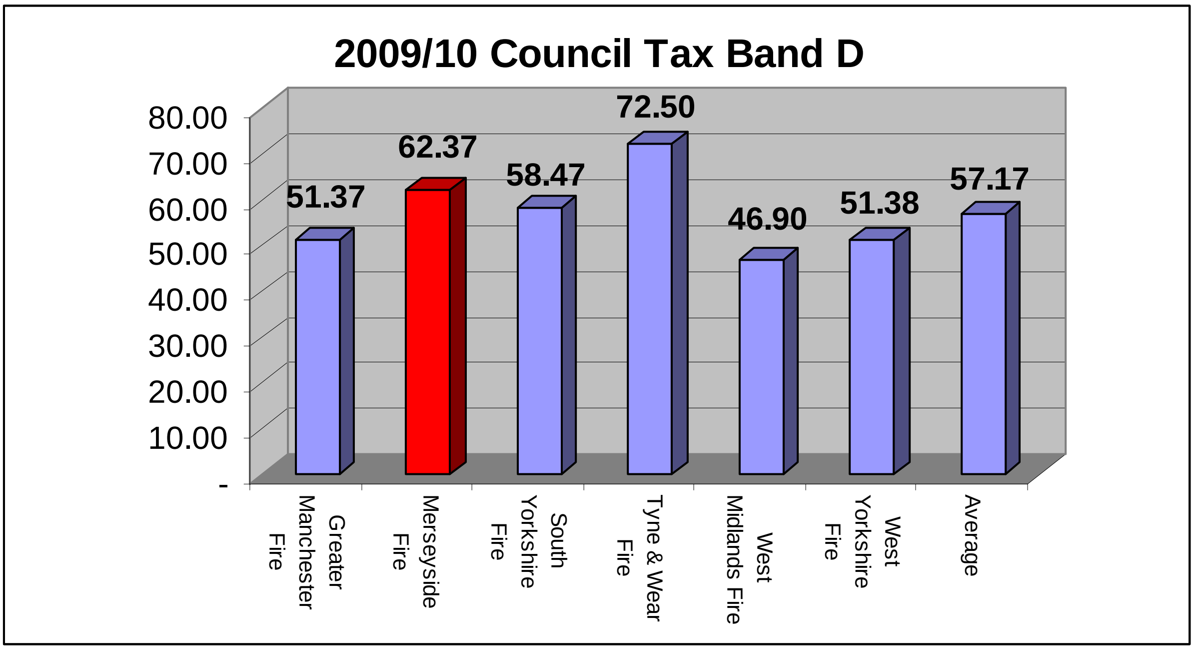
- Sought to minimise council tax increases with a target increase of less than 4% that it has adhered to despite severe financial constraints;
- Planned for pay awards and grant increases in line with HM Treasury medium term expectations;
- Recruited to meet the Authority's high performance standards and budgeted for staff actually in post;
- Sought to generate significant savings through staff reductions whilst avoiding compulsory redundancy;
- Made significant investment in Community Fire Safety and preventative work. (REDUCE);
- Invested to maintain emergency response standards and to modernise working arrangements for dealing with a whole host of emergency incidents. (RESPONSE);
- Developed arrangements for restoration with the private sector and the Fire Support Network. (RESTORE);
- Made significant investment in IT and computing (including outsourcing);
- Provided further investment in equality and health and safety;
- Attempted to plan prudently for over the medium term by considering all significant risks to the assumptions in the financial plan and creating specific reserves if deemed necessary;
- Maintained a general fund reserve of at least £2m following assessments of risk;
- Because of pressures on revenue budget generally avoided funding capital expenditure from revenue through leasing or RCCO;
- Invested in the capital infrastructure of the Authority in line with Asset Management Plan, vehicle replacement strategies and corporate objectives.

37. These strategies have allowed the Authority to make significant strides in reducing cost and maintaining relatively low levels of Council Tax increase despite very tight grant settlements. It should especially be noted that in 2006/07 the Authority within its 5 year plan adopted a significant three years savings strategy to address an underlying gap between expenditure and income following a change in the grant formula relating to Firefighter Pension Funding. Following the poor grant settlement for the period 2008/09 – 2010/11 (1.0%, 0.5%, and 0.5%) a further saving strategy was developed to deliver £5.0m saving by 2011/12. This is discussed in more detail later in the report.

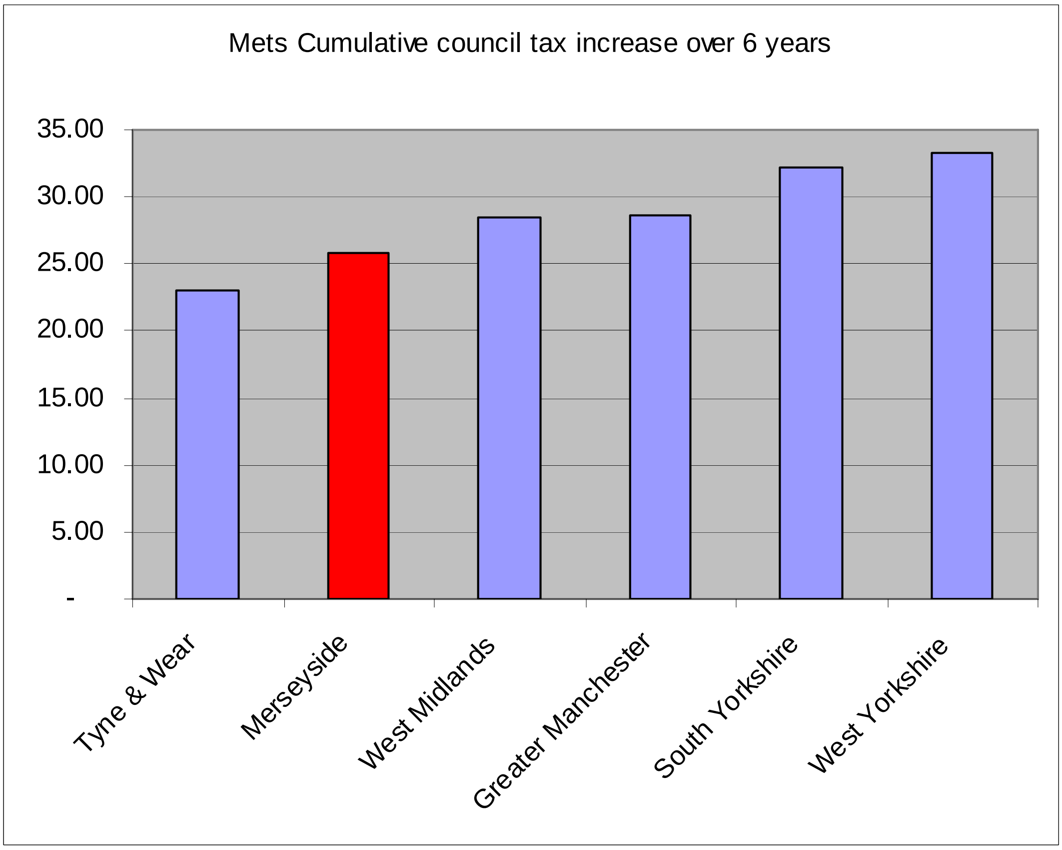
38. The Authority is below the national average council tax for fire services.



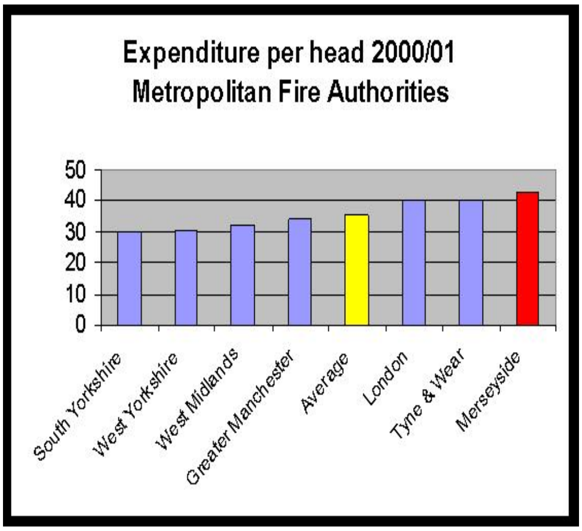
39. In 1996/97 Merseyside Fire & Civil Defence Authority Council Tax was more than 50% above the average of Metropolitan Fire Authorities. Now it is only 9% above the average:

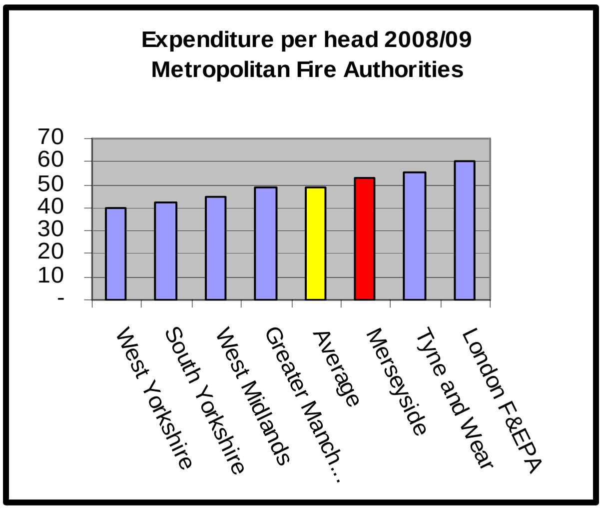


40. Over the past 6 years when compared to the other metropolitan fire authorities Merseyside has had one of the lowest cumulative council tax increase:

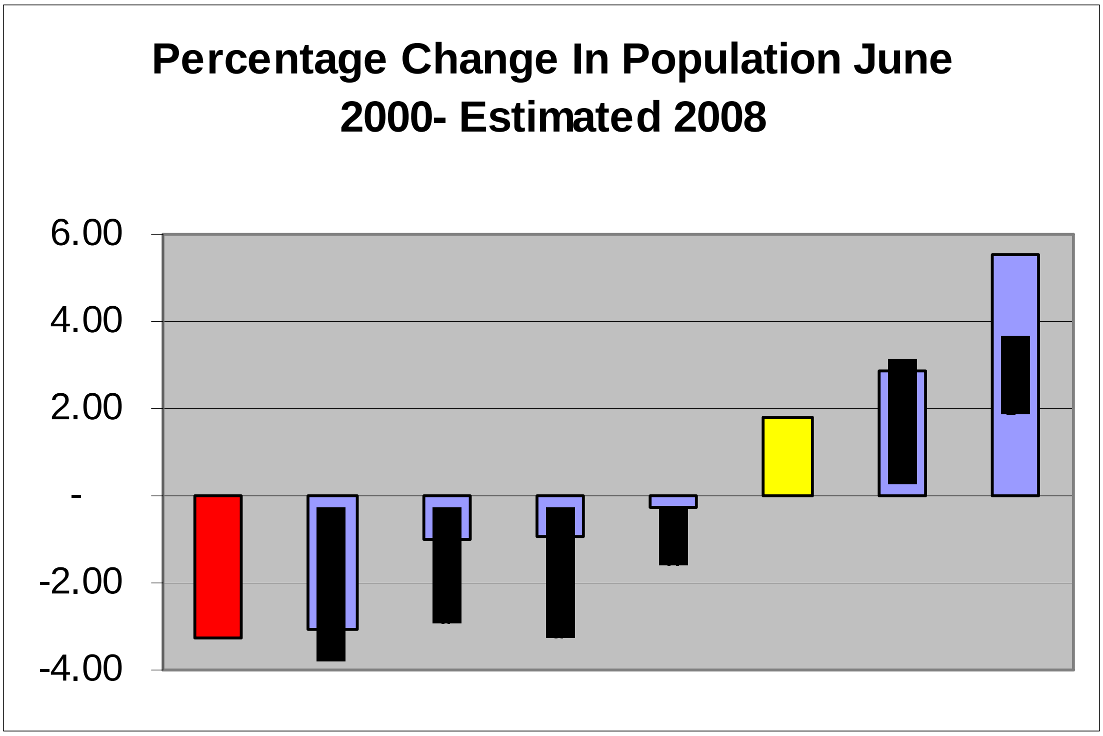


41. The significant improvements in efficiency by the Fire Authority and a large scale savings plan have meant that from being the most expensive metropolitan Fire Authority in the country in 2000/01 the Authority has moved to being only the third most expensive metropolitan Fire Authority by 2008/09.

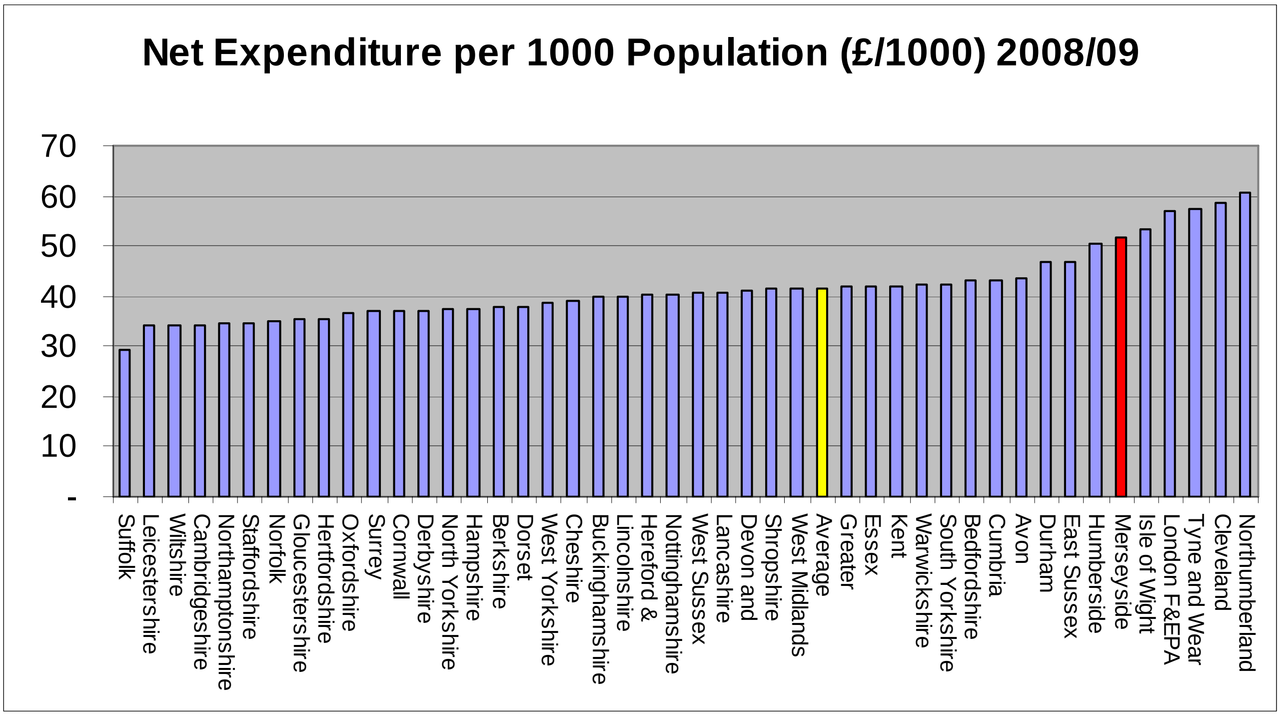




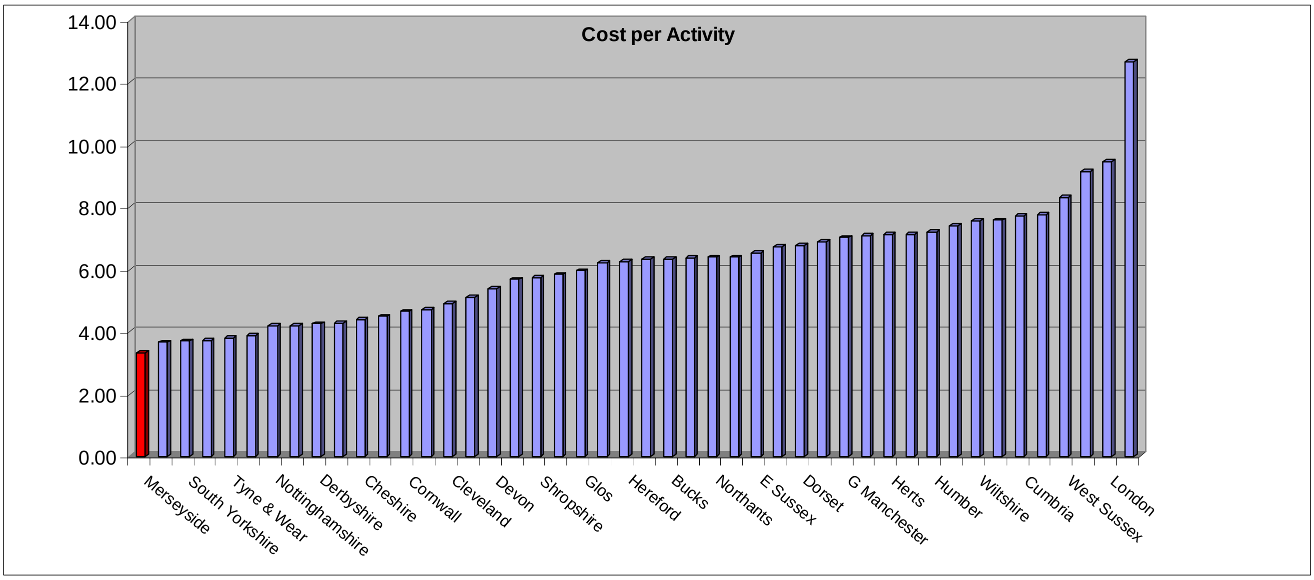
42. This performance has been especially encouraging when it is considered that across the same time period the population of Merseyside has been reducing significantly whilst other Authorities populations have grown. *If all other things has been equal it might have been expected that Merseyside's position might have worsened on this comparator rather than improved.*



However, despite the recent improvements it should be noted that we remain, in comparison to our peers, a relatively high spending authority on a direct expenditure per head basis.

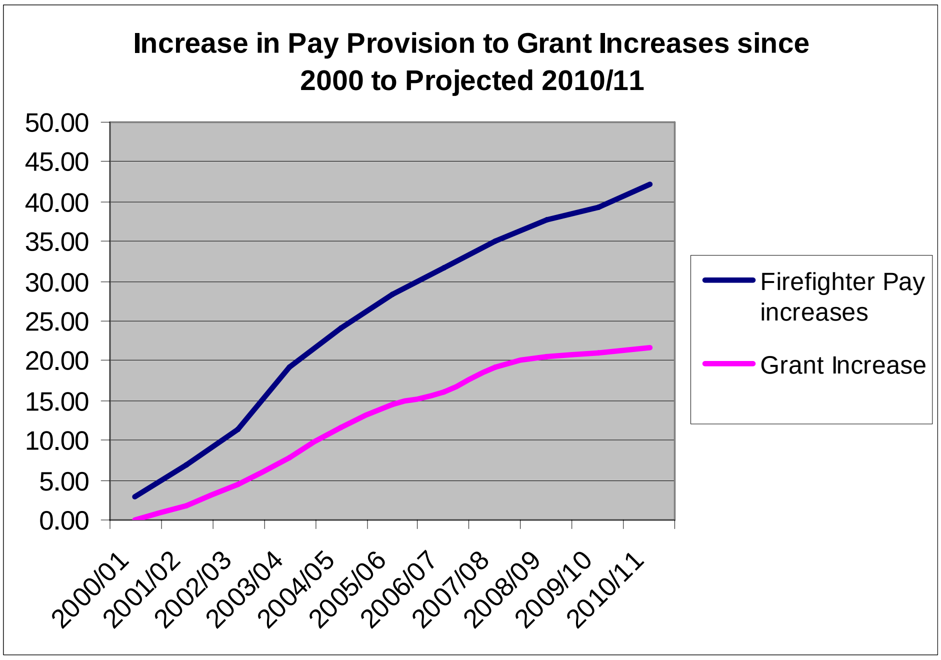


However it is noted that that this is only one measure of the relative need to spend (population basis). The Executive Director of Resources has analysed available data and compiled a comparison of net expenditure to activity (including home fire safety checks). This clearly shows a very different picture:



43. Merseyside continues to invest significantly in community fire safety, approximately £6 million in 2009/10. (This does not include the massive investment in smoke alarms and the fire safety work undertaken by stations)

44. These improvements in Council Tax level and expenditure have been achieved when the Authority's grant increases have been at the floor (minimum) level for many years whilst inflation including Firefighters' pay awards have been very much higher. The table below highlights cumulative grant increases compared to cumulative pay awards since 2000 and the projected 2008 -20011 position (in line with the medium term financial assumptions around pay provision increases of 2%p.a. and actual grant increases).



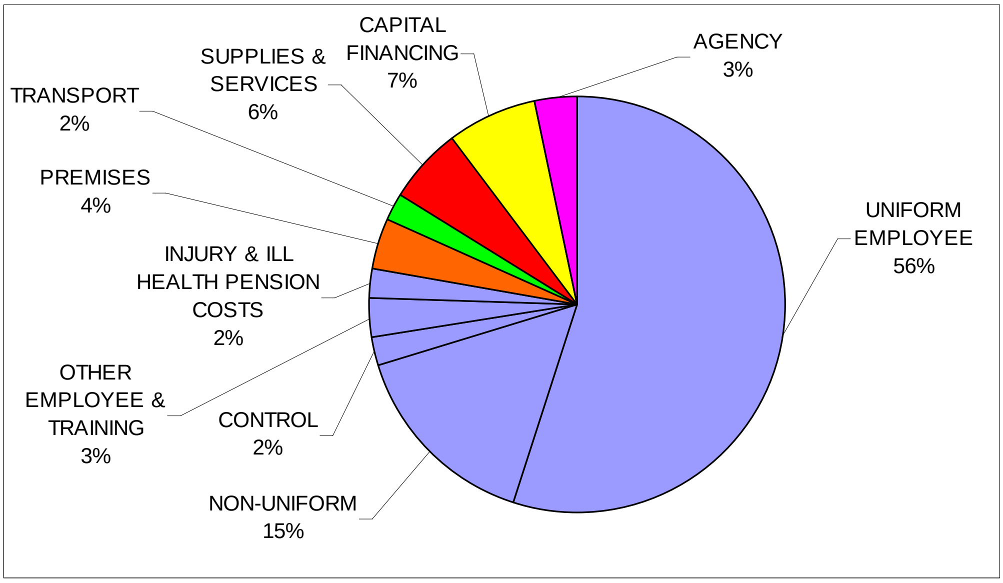
Overall Financial Health

45. The overall financial position of the Authority appears relatively good on the basis of the following key indicators:-

- Under the new and much tougher Comprehensive Area Assessment – Use of Resources Assessment the Authority scored a 3 in all three themes indicating it continues to exceed the minimum requirements and is performing well.
- Authority accounts 2008/2009 audited without qualification again.
- Annual Audit letter highlighted general satisfaction with financial corporate governance and reporting arrangements.
- IRMP recognised as innovative.
- The Authority has maintained a general revenue reserve of at least £2.0m in recent years.
- Cost centre budgeting now well established.
- Maintained a five year financial plan and capital programme and most importantly a consistent medium term strategy.
- The Authority has delivered huge efficiency savings (see detailed revenue section) which have been highlighted as best performance in the recent Audit Commission national report "*Rising to the Challenge……improving fire service efficiency*".

Current Allocation of Resources

46. Members will be aware that Fire Service expenditure is predominantly on employee related costs (c80%) as is shown in the pie chart below. (The blue sections relate to employee costs)

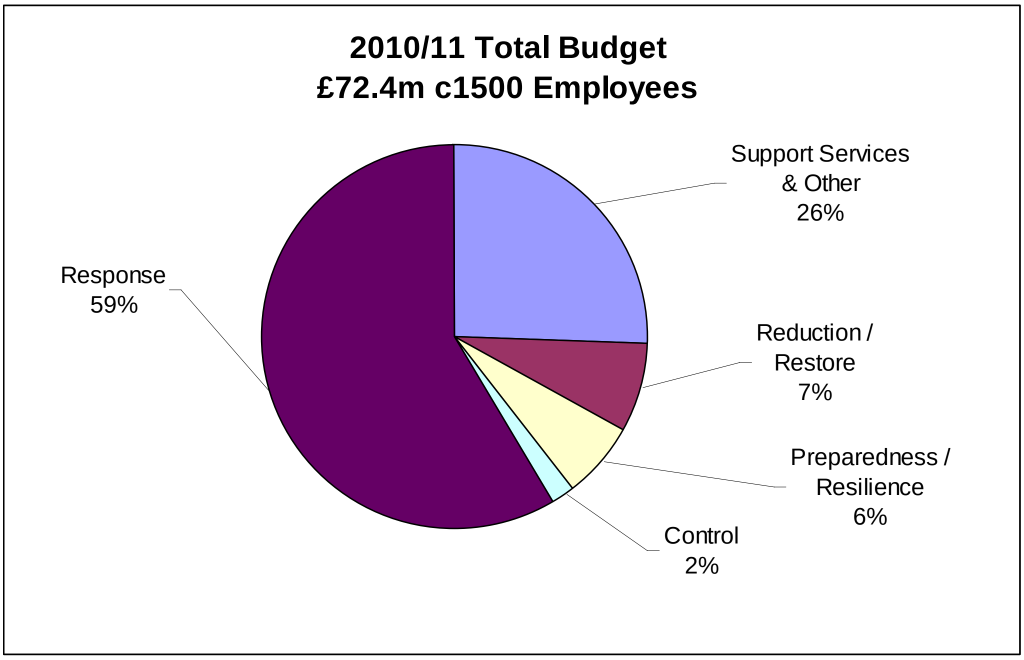


A full subjective analysis of the budget is set out in **Appendix 1**

47. A subjective analysis is only part of the overall view on spending and in order to assist Members the same data is shown in a “thematic” view below based upon the strategic objectives.

Allocation of Resources in line with Corporate Objectives

48. The Authority has an excellent track record of investing in line with its corporate priorities and this was reflected in the CAA and UoR scoring process. It can be seen from the pie chart below that over 59% of expenditure goes on emergency and specialist response, 2% on Control Rooms and 13% on Fire Resilience & Reduction. Support costs making up the remaining 26%.



Looking in more detail at each area the following investments are included:-

Reduce & Restore

49. Investing over £5m p.a in fire safety including:

- Employment of 48 specialist Advocates (£1m)
- Purchase of £0.7m worth of smoke alarms.
- Continuation of the Princes Trust and Free Programmes (£0.1m).
- Investment in an Arson Task Force (£0.4m)
- Investment in Fireworks Team (FIRST) (£0.1m)
- Investment in District Fire Safety Teams (£1.4m)
- Fire Service Direct (£0.2m)
- Working with young people, including school liaison.
- Invested in volunteers with the Fire Support Network (£0.2m)
- Working with the private sector to deliver speedier restoration of property

Responding & Control

50.

- Service delivery and emergency response through its 26 fire stations (these staff do increasing amounts of preventative work as well).
- Specialist teams like Search and Rescue Team, Targeted Response Group, Hazmats Team and Emergency Response dogs
- Invested in staff safety – procured the highest specification in terms of fire kit, helmets, boots and appliances
- Invests in two small fires unit, targeting antisocial fires.
- Invests £0.4m on the Incident Management Team.
- Developed the unique quick response motorcycle unit.
- Deliver 100,000 HFSC's p.a.

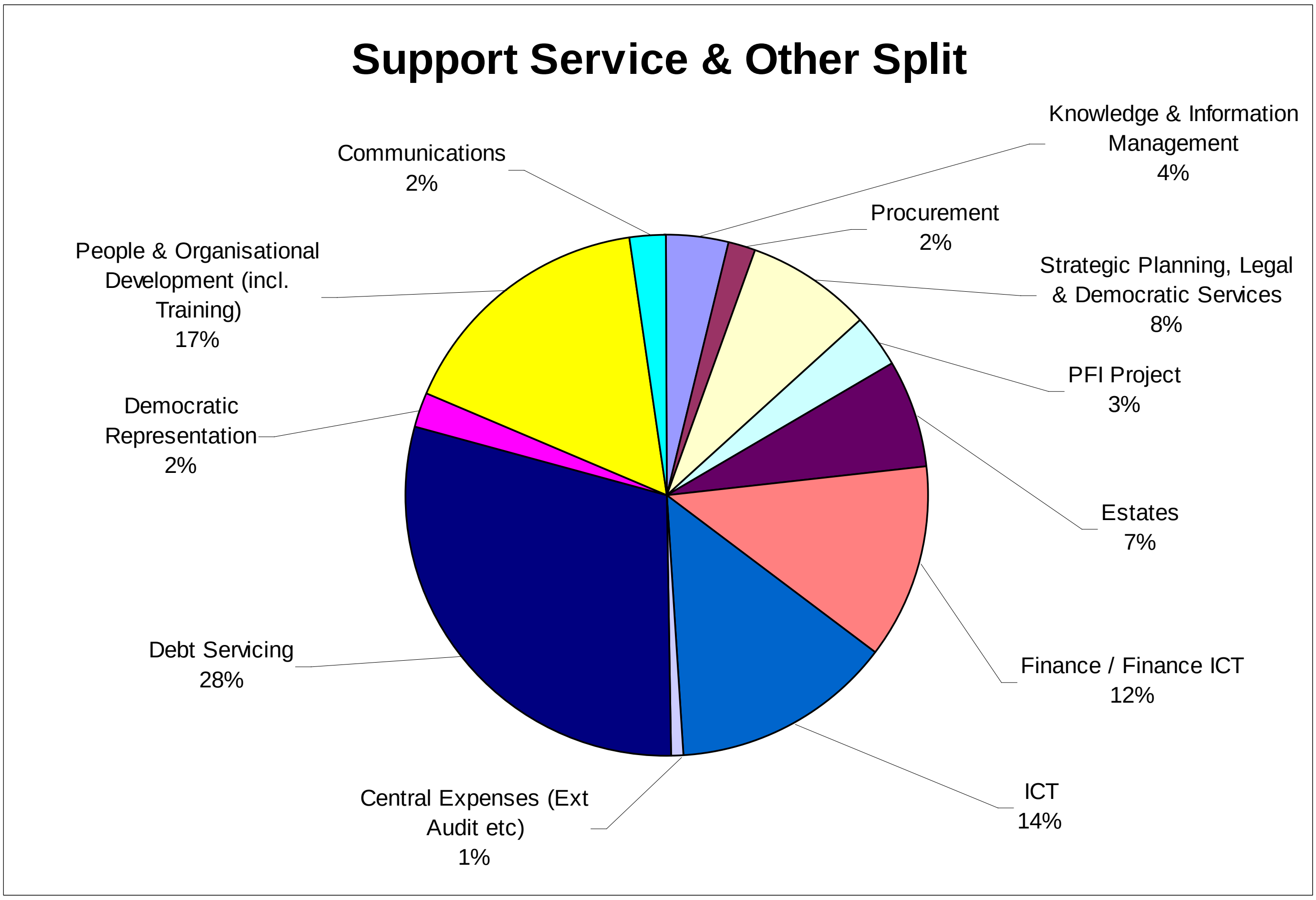
Preparedness & Resilience

51. The investment of £4m delivers a variety of services which helps support and complement the front line response investment and ensure Firefighter safety.

- Operational Planning and Policy
- Contingency Planning
- New Dimensions to cope with major disasters and terrorist threats
- Operational Equipment Team
- Water Section
- Health and Safety Department
- Transport/Fleet Management – to keep vehicles operating effectively
- Workshops
- Marine Rescue Unit to support the airport and safety on the river
- Standard Operating Procedure Review Team

Support Services & Other

52. The investment in support services of £18m (26% of the budget) is analysed below:



It should be noted that:-

- People and Organisation Development – includes investment in the Training and Development Academy and costs of training for all staff;
- Debt Servicing Costs – reflect the investment in asset purchase and improvement in the past;
- Estates – includes the running costs of buildings;
- ICT – includes the cost of the Mobilising Command and Control System;
- Strategic Planning / Legal Services – includes the cost of insurance and claims;
- Finance – includes the cost of managing and maintaining the corporate finance system.

Members need to assure themselves that the Authority continues to allocate resources to support its strategic priorities. They will note that the Budget Working Group have reviewed the base budget in detail.

(C) CAPITAL PROGRAMME

53. Capital is considered first in this report so that Members can clearly consider the revenue impacts of capital investment and borrowing decisions as part of revenue budget and Council Tax considerations.

Introduction

54. The Government in consultation with the Chartered Institute of Public Finance (CIPFA) has, over the last few years, been reviewing the capital control system of local government, with a view to improve accountability and freedoms for local authorities in respect of capital investments. In effect, it has been seeking to allow "business" based decisions whilst retaining overall control of public spending.

55. From 1st April 2004, the Local Government Act 2003 replaced the previous regime of capital controls, as set out in Part IV of the Local Government and Housing Act 1989, with the Prudential System of Capital Finance.

56. Under the previous system of capital controls local authorities were only permitted to finance capital expenditure from borrowing within limits set by the Government (Credit Approvals). The new arrangements enable local authorities to decide for themselves how much they can afford to borrow for capital purposes, subject to various safeguards. The Government has reserve powers to limit an authority's borrowing if the Government believes it to be unaffordable, or in times of public spending restraint.

Prudential Code

57. A key part of the new capital system is the CIPFA "Prudential Code for Local Authority Capital Finance" which provides a framework of decision-making under which authorities will decide their capital investment and financing plans and set limits for borrowing.

58. Authorities will be required to 'have regard to' the Prudential Code when setting their future budgets and Council Tax levels - which in practice means that they would need to have very good reasons not to comply.

59. The over-riding objective of the Prudential Code is to ensure that the capital investment plans of local authorities are **affordable, prudent, sustainable**, and follow good practice.

60. Some of the main features of the Prudential Code are as follows:

- The full Authority must consider and set a number of indicators and limits for its capital plans as part of the annual budget setting process. The limits can be revised during the year but only by the full Authority. The mandatory indicators are shown in section E.

- The indicators and limits must be monitored during the year and outturn figures reported.

- The Authority must produce and maintain capital and revenue plans for at least three future years including three year estimates of its future Council Tax taking account of the proposed capital programme and other plans.

- The Authority must set an authorised limit for its total debt (including borrowing and long term liabilities) which may not be exceeded.

- Limits relating to treasury management matters must be considered as part of the Annual Treasury Management Strategy Report.

61. Fundamentally, the objective of the Code is that the total of an authority's capital investment remains within sustainable limits, following consideration of the impact on the "bottom line" Council Tax. This is ultimately determined by a judgement about what Members consider is an acceptable level of Council Tax.

<u>Capital Investment Strategy</u>

62. Each financial year the Authority produces a capital programme to manage major capital schemes. Owing to the nature of capital expenditure a large number of schemes span more than one financial year so the programme is a rolling programme covering five future financial years.

63. The starting point for this programme has been an assessment of the capital spending requirements for the Authority for future years based upon needs identified by the various expert professionals in areas like buildings, vehicles, ICT, and operational equipment. Initial bids were requested and through an iterative process Officers have modified the programme in the light of:

(a) service requirements, and in particular investments required to support and deliver the IRMP.

(b) the need to adopt a prudential approach to capital borrowing under the new regime, being mindful of affordability, prudence and sustainability and in particular the impact on Council Tax levels.

64. This has produced a total 2010/11 – 2014/15 five-year future capital programme proposal of £36.776m which is set out in the summary table overleaf. This table also identifies funding of the programme and hence the borrowing requirements to support that capital programme. The full programme is set out in **Appendix 2** (appendix 2A is the updated programme and appendix 2B the proposed new starts).

2010 - 2015 Proposed Capital Investment

Type of Expenditure	Total Cost £	2010/11 £	2011/12 £	2012/13 £	2013/14 £	2014/15 £
Building/Land	**8,868,000**	5,745,500	816,000	1,005,500	306,000	995,000
Hydrants	**185,000**	37,000	37,000	37,000	37,000	37,000
Fire Safety	**8,762,000**	1,752,000	1,752,000	1,752,000	1,752,000	1,754,000
ICT	**2,170,000**	603,000	373,000	328,000	333,000	533,000
RCC - ICT investment	**70,000**	50,000	20,000	0	0	0
Operational Equipment	**951,700**	676,700	20,000	195,000	20,000	40,000
T.D.A.	**110,000**	110,000	0	0	0	0
Vehicles	**8,622,600**	2,978,400	1,553,600	1,008,600	1,672,800	1,409,200
Fire World	**7,035,000**	0	0	3,560,000	3,475,000	0
TOTAL	**36,774,300**	**11,952,600**	**4,571,600**	**7,886,100**	**7,595,800**	**4,768,200**
Financing Available:	**Total £**	**2010/11 £**	**2011/12 £**	**2012/13 £**	**2013/14 £**	**2014/15 £**
Capital Receipts	900,000	900,000	0	0	0	0
External Contributions	6,035,000	0	0	3,060,000	2,975,000	0
R.C.C.O.	5,000,000	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Grant	1,072,000	1,072,000	0	0	0	0
	13,007,000	2,972,000	1,000,000	4,060,000	3,975,000	1,000,000
Borrowing Requirement						
supported	16,899,347	3,251,000	3,316,020	3,382,340	3,449,987	3,500,000
unsupported	6,867,953	5,729,600	255,580	443,760	170,813	268,200
Borrowing	23,767,300	8,980,600	3,571,600	3,826,100	3,620,800	3,768,200
Total Funding	36,774,300	11,952,600	4,571,600	7,886,100	7,595,800	4,768,200

Members will note that the plan includes a small amount of new starts/additions,. These are:-

(a) The addition of the extra year to the programme 2014/15, £4.768m
(b) New starts in 2010/11 – 2013/14, £1.172m

65. These projects represent additional investments which are considered as essential by CLT following detailed review of bids submitted by Officers. They include investments in line with supporting strategies and programmes agreed by the Authority already. Details of the new starts can be found in Appendix 2B attached to this report, and an outline of the scope of each of the main capital programme divisions is presented below. Appendix 2A provides a full analysis of the updated approved 5 year capital programe and also report CFO/012/10, elsewhere on the agenda, details the movements on the approved capital plan. These schemes have been considered in detail by the Budget Working Group as part of the budget process.

66. The key assumptions underpinning the five year capital programme, (2010/11 - 2014/15) are:-

(a) <u>Building Investment Strategy (£8.869m)</u>

67. The estate comprises 26 fire stations, a training and development academy (TDA), Workshops, a Mobilising & Control Centre (MACC), Service Headquarters and the new Engineering Centre development. The capital programme reflects the funding required to replace, maintain and enhance the current estate stock, and when possible seeks to attract external funding (PFI) or specific contributions (capital receipts, capital reserves) to reduce the level of borrowing requirement. Estates are finalising the revised and updated 5 year property asset management plan and the proposed capital programme is consistent with the priority areas that will be contained within the plan.

<u>PFI</u>

68. In order to address the investment required, Officers submitted a successful PFI bid for the Fire Service. The Government has approved a joint project (with Merseyside leading), between Merseyside, Lancashire and Cumbria. In Merseyside there will be new fire stations at Birkenhead, Kirkdale, Southport, Newton-le-Willows, Belle Vale, Bootle and Formby.

69. The total capital building costs for the North West building stock will be £45.4m and in Merseyside £19.8m. As the capital expenditure will not go through the Authority’s capital programme (and the contract has yet to be formally signed) this scheme is not included in the current capital programme. Changes to the accounting rules will mean that in the future the PFI assets will be on the Authority’s balance sheet and the necessary adjustments will be made to the MRP and prudential indicators (this will simply reflect a technical accounting adjustment).

<u>Non PFI Project Assets</u>

70. For those properties which don’t form part of the PFI project investment is proposed in line with the current Asset Management Plan. Notably :-

- Refurbishing and essential work at fire stations £5.2 m
- LLAR accommodation £0.7m
- New Kensington Community Fire Station £1.8m
- Marine 1 Accommodation £0.3m

(b) Non Operational Equipment & Hydrants (£0.185m)

71. The regular annual provision is made for installation of new or replacement hydrants in line with our water strategy, £0.2m.

(c) Fire Safety (£8.762m)

72. Smoke alarms and sprinkler systems are being classed as capital expenditure in line with Government guidance. This follows the awarding of capital grants by the ODPM towards the purchase cost of such items in financial years 2004/05 through to 2007/08. The estimated cost of purchasing alarms over the 2010/11 – 2014/15 period is £3.7m, approximately 100,000 alarms p.a. Current policy is to capitalise the installation costs of smoke alarms estimated at £5.0m over the period, however this expenditure is not funded through borrowing but financed in the year by a revenue contribution to capital.

(d) ICT – Investing in line with the ICT Strategy (£2.170m)

73. In line with the Authority's commitment to using technology to improve the service there is a significant investment in ICT within the programme. The most significant investments are in line with a phased introduction of a controlled planned replacement policy of 5 years in the area of PCs, Servers and Network £1.2m, and software licenses £0.5m.

Specific projects include:-

- developing Knowledge Management Systems, £0.2m,
- development of utilisation of new emerging technologies £0.1m

(e) Regional Control Room (RCC) – associated ICT Investment (£0.07m)

74. Officers have identified projects associated with the challenges of operating within the information environment associated with the RCC and the need to retain some information resilience in-house post the RCC:

- ICT Security, £0.07m – The current application for managing the calls to the Authority and the requests for non-fire emergency work needs to be replaced and improved. Post RCC the Authority will still need a system to manage this work.

(f) Operational Equipment (£0.952m)

75. Significant provision is also made to ensure that a modern fire and rescue service can be delivered and in particular provision is made for investment in specialist rescue equipment and new breathing apparatus, particularly:-

- Hydraulic rescue equipment £0.2m
- Water rescue equipment £0.1m
- Provision for the purchase of a hovercraft £0.1m

(g) Training & Development Academy (£0.1m)

76. The development and construction of a hazardous materials training rig, £0.1m to keep the TDA up to date and efficient for training purposes.

(h) Vehicle Replacement Strategy (£8.623m)

77. The Fleet Manager has identified needs as follows:-

An Ageing Fleet

78. The Authority has developed an appliance replacement strategy based on the economic life of an appliance. Each appliance has an estimated service life of 8 years on the front line followed by 2 years as a reserve appliance. Significant provision for new appliances has been included in the capital programme – up to 24 new appliances (approximately 5 appliances per year) to ensure that the fleet is modern and efficient. These purchases will also help introduce the rescue pump/support pump concept - see below for details.

A Need for Specialist Vehicles

79. There is a need to make provision for the purchase of specialist vehicles to support the IRMP and to support the wider range of roles for the fire service including rescue:

- Rapid Response Motorbikes
- Combined pump platform appliances
- SFU vehicles
- Prime movers

Ancillary Vehicles

80. Provision is included for the phased renewal of the ancillary vehicle fleet. These are increasingly important to support the Fire Safety work referred to in c) above.

(i) Fireworld (£7.035m)

81. Total provision is made of £7m for developing a world leading community education centre and visitor attraction. It is assumed that the Fire Authority would only have to fund £1m of this with the remainder of the investment provided by partners. The scheme is still in the early stages of development and members would receive a full report on the project and a detailed business case before the project is developed any further.

Funding The Programme

Capital Receipts

82. Capital receipts are usually the proceeds from the sale of assets. Any such receipts can be applied either to reduce an authority's outstanding debt or to be reinvested in the capital infrastructure.

83. The Authority has (when available) used capital receipts as a source of funding for new capital investment with little, if any, being used for debt repayment – unless regulations require a proportion of the receipts to be used specifically to repay debt. However, under the new regime the Authority needs to consider whether a proportion of any future receipts should now be used for debt repayment, and thereby ensure that the cost of debt financing does not increase for future Council Tax payers.

84. The proposed capital programme anticipates capital receipts only from: -

Low Hill Fire Station site	£0.25m	(2010/11)
Old Workshop site	£0.65m	(2010/11)

85. It assumes that this receipt will be used to reinvest in the capital infrastructure. Members should note that the valuations of the receipts are based on the early part of 2008 since when the commercial property market has slumped. Officers are monitoring markets closely and will report on the timescales for proposed sales.

Capital Grants

86. Members will recall that the CSR07 announced fire authorities would receive a grant towards the cost of capital investments in 2009/10 – 2010/11. On the 15 December 2009 CLG announced the Authority would receive a capital grant of £0.805m and £1.072m in 2009/10 and 2010/11. As the Authority already has an approved 5 year programme covering the period associated with this grant it has been assumed that the Authority will reduce the level of borrowing originally anticipated for this period in the programme by utilising the grant to fund planned spend.

Partner Contributions

87. Partner contributions (either grant, sponsorship or capital receipts) are anticipated for Fireworld, £6m.

Alternative to Operating Leasing

88. Under the previous system of capital controls, investment that was funded by operating lease did not count as either capital expenditure or the financing as a credit arrangement. Therefore, in common with most other local authorities, operating leasing has been a source of funding for some limited eligible assets (e.g. vehicles, plants and machinery, and computer equipment) although the Authority generally avoided this because of the impact on the revenue account. However, whilst operating leasing as a source of funding remains outside of the Prudential capital system, no leasing is assumed in this programme. The Executive Director of Resources will monitor the suitability of alternative methods of finance.

Borrowing

89. Under the Prudential capital system Local Authorities are now able to increase their borrowing above the allocation provided by the Government to fund capital investment. However, the Government has retained reserve powers to limit an authority's borrowing if the Government believes an authority's proposals to be "unaffordable" or in times of national public spending constraint.

90. The proposed capital programme represents an overall expenditure increase of £5.9m reflecting the proposed "new starts" expenditure (of which £4.8m relates to extension of rolling programmes into the additional programme year- 2014/15). Appendix 2B sets out the new start schemes.

91. The impact of the new start programme on the Authority's borrowing is a net increase of £4.940m to £23.767m:

	£m
Increase in expenditure, new starts	5.9
Increase in Non Borrowing Funding Sources:	
• RCCO (HFSC installation costs)	-1.0
Required Increase in Borrowing	4.9

This level of supported borrowing for the Authority across the five year period is estimated to be £16.9m.

The level of prudential "unsupported" borrowing is therefore:-

	£m
Total borrowing in programme	23.767
Supported Borrowing Estimate	16.899
Total "Prudential Borrowing"	6.868

Impacts on Revenue Budget and Financial Plan

92. When the Authority borrows money it has to factor the debt repayment and interest costs into its financial plans. The minimum revenue provision (MRP) methodology calculates how much debt repayment is required each year. Following the new Capital Regulations announced in 2008 the Authority must approve an MRP Statement each year that sets out the policy on MRP. Section D of this report outlines for Members the proposed MRP policy for 2010/11 – 2014/15 and the methodology for calculating the MRP. The additional borrowing and proposed MRP policy require an increase to the 2009/10 base figure for MRP & Interest of:-

	2010/11 £m	**2011/12 £m**	**2012/13 £m**	**2013/14 £m**	**2014/15 £m**
Increase in MRP/Interest	0.458	0.703	0.999	1.388	1.917

This increase has already been built into and planned for in the current approved MTFP. To give Members an indication of the impact of the proposals in isolation, rather than the marginal impact on the financial plan, the following table has been prepared:-

	If Borrowing was restricted to the level of **Supported Borrowing**
Reduction in Borrowing	£6.868m
Reduction in Unsupported Debt Repayment costs	£0.875m
Council Tax equivalent	3.3% or £2.08

More information on the impact on the Capital Programme is shown in the section on Prudential Indicators (section E).

(**D**) **MINIMUM REVENUE PROVISION STATEMENT**

93. Under the Local Authorities and Accounting Regulations the Authority is required to set aside a sum of money each year to reduce the overall level of debt, this sum is known as the Minimum Revenue Provision (MRP). The 2003 regulations set a minimum annual amount to be charged to revenue based on the Authority's Capital Financing Requirement (CFR) which is an amount broadly equivalent to the Authority's outstanding debt. The regulations have been updated in 2008 and now require each authority to repay debt at a rate it considers **prudent** and to set out in an annual statement the Authority's policy on making MRP in respect of the forthcoming year.

94. The new regulations guidance interprets MRP may be deemed to be prudent if it is either:

- Based over a period that is reasonably commensurate with that over which the capital expenditure / asset provides benefits (asset life), or

- For the element of expenditure met from borrowing supported by government Revenue Support Grant (RSG), a period reasonably commensurate with the period in the determination of that grant (this in reality would equate to the current 4% MRP methodology)

95. The regulations guidelines set out four options for calculating MRP, they are summarised below:

- **Regulatory Method** – MRP is equal to the amount determined in accordance with the former regulations 28 & 29 of the 2003 Accounting Regulations – the MRP element of the Revenue Support Grant is calculated on this basis. This method has been used to determine the Authority's 2007/08 and 2008/09 MRP for both supported and unsupported borrowing**.** With effect from 2009/10 this method of determining MRP is only available for capital expenditure that is funded by supported borrowing.

- **Capital Financing Method** - MRP is based on 4% of the CFR. From 2009/10 this option will only be available for capital expenditure that is funded by **supported borrowing**.

- **Asset Life Method** – MRP is determined by reference to the life of the asset and the amount is either based on equal instalments over the period or on an annuity method based on assumed principal repayments. This option is available to both supported and unsupported borrowing in determining the MRP requirement.

- **Depreciation Method -** MRP is to be equal to the provision required in accordance with depreciation accounting in respect of the asset on which expenditure has been financed by borrowing. This option is available to both supported and unsupported borrowing in determining the MRP requirement.

<u>2010/11 MRP:</u>

96. The 2010/11 MRP is determined by the actual level of **outstanding debt (CFR) as at the end of <u>2009/10</u>.** Any 2009/10 expenditure funded through unsupported borrowing must have the associated MRP requirement determined by either the Asset Life or Depreciation method.

<u>Proposed MRP Statement 2010/11:</u>

97. For capital expenditure incurred before 1st April 2008 and for future **supported** capital expenditure - MRP will be based on the Regulatory Method as this:

    (a) Consistent with the current and previous approved financial plans and does not adversely impact on 2009/10; and

    (b) Is deemed prudent for current and future supported borrowing as the charge to revenue for MRP is commensurate with the period and funding associated the Revenue Support Grant.

98. For capital expenditure incurred **after 1st April 2008** and financed by **unsupported** borrowing MRP will be based on the Asset Life equal instalment method. This option meets the requirements to be deemed prudent but also allows certainty and predictability over MRP charges.

Expenditure Funded by Supported / Unsupported Borrowing:

99. The Authority in the past has determined it can afford and sustain significant prudential unsupported borrowing in order to allow the required level of investment in the infrastructure and assets of the Authority to deliver a modern well equipped fire service. The prudential borrowing was not associated with specific projects, it simply reflected the total borrowing required to fund the investment in the 5 year capital programme.

100. The table below identifies that the 2009/10 programme requires £3.1m of unsupported borrowing and in order to determine the MRP (based on asset life) for 2010/11 the unsupported borrowing must be “earmarked” against schemes in the programme.

	Total	**2009/10**	**2010/11**	**2011/12**	**2012/13**	**2013/14**	**2014/15**
	£	£	£	£	£	£	£
Borrowing Requirement							
supported	20,059,347	3,160,000	3,251,000	3,316,020	3,382,340	3,449,987	3,500,000
unsupported	9,977,625	3,109,672	5,729,600	255,580	443,760	170,813	268,200
Total	30,036,972	6,269,672	8,980,600	3,571,600	3,826,100	3,620,800	3,768,200

101. In order to determine the prudential / unsupported associated assets within the proposed capital programme the following approach has been used:

- Schemes in the approved programme (excludes any new starts schemes) would have the supported borrowing allocated to them in the first instance, then;
- If the level of the approved programme in any year exceeded the available supported borrowing, the sub-groups (building, ICT, vehicles etc) would be put in priority order and supported borrowing allocated on that basis;
- This would then leave the schemes funded by unsupported borrowing and the asset life would be known and allow the MRP to be determined.

102. Officers have therefore allocated the supported borrowing against the core assets in the programme and those required to deliver the Authority’s vision. This process is required to calculate the MRP provision and should not be taken as anything more. Priority has been made in the following order:

Priority For Earmarking Supported Borrowing Against Schemes:

Rank	Type of Expenditure	Rationale For Priority
1	ICT & Vehicles	Require ongoing replacement & investment to provide service with tools & information to deliver core business
2	Operational Equipment	Require ongoing replacement & investment to provide service with tools to deliver core business
3	Buildings	Important investment area but enhancements/ replacements could be deferred IF Government withdrew prudential regime
4	CFS equip & installation	Majority of current spend funded by non-borrowing. IF prudential borrowing was not available then the Authority is likely to continue spend but fund it through unsupported borrowing or revenue contributions
5	Other	The likes of Fireworld may be seen as important investments in selling the vision & message of the Authority, but funded through prudential / unsupported borrowing if the business case and benefits are worthwhile.

The financial plan outlined in this report reflects the proposed Authority's policy on prudential MRP.

(E) PRUDENTIAL INDICATOR REPORT

103. Having formulated a draft Capital Programme, the Authority, in making final decisions upon that Capital Programme and Revenue Budget 2010/11, will need to consider a report setting out a range of Prudential Indicators aimed at demonstrating the intended Investment Programme's affordability, prudence and impact upon Treasury Management activity and strategy.

104. It should be noted, however, that in order to provide those Indicators, both Capital and Revenue financial plans need to be prepared for each of the next 3 financial years, commencing with 2010/11.

105. The financial plans prepared in respect of the financial years 2011/12 and 2012/13 are not to be mistaken for approved Budgets. They are, at this stage, only a guide for financial planning and as such subject to significant change as a result of decisions made by the Authority. However, such plans are required to be supported by an indication of future Council Tax. At this stage an assumption of Council Tax increases of 4% in all years has been made.

Prudential Indicators

106. The Authority must demonstrate that its spending plans comply with the Prudential Code by the publication of a number of performance indicators, which are known as the Prudential Indicators*.* ***Details of the prudential indicators for this Authority are provided below.***

107. The purpose of the indicators is to demonstrate that capital investment remains within sustainable limits and that the Authority has considered the impact of the whole plan on future levels of Council Tax. The indicators that will measure this are:-

- Estimates of the ratio of capital financing charges to the net revenue budget
- Estimates of the precept that would result from the three-year capital plan.
- Estimates of the capital financing requirement.

Decision Making on Capital Investment

108. A fundamental principle of the code is that the capital programme must be driven by the desire to provide high quality value-for-money services. As a consequence the code explicitly recognises that in making its capital investment decisions the Authority must have regard to options appraisal, asset management planning and the strategic aims of the Authority.

109. In compiling this capital plan each of the schemes has been measured against both the strategic aims of the Authority and in line with the IRMP. In addition under financial procedures Officers cannot commit expenditure on capital schemes without first submitting a business case to either the Corporate Leadership Team or Strategy and Resources Committee depending upon the size of the scheme.

2010/2011 Supported Capital Expenditure Allocations

110. Under the old system of capital finance the amount of Basic Credit Approval was supported by revenue support grant as part of the annual settlement. Under the new procedures this support is maintained and each Authority is notified of the amount of capital expenditure which will be supported by revenue support grant. The amount for this Authority notified for 2010/2011 is £3.251m, an increase of £0.091m on 2009/10. The 2011/12 and 2012/13 figures have been estimated at £3.316m and £3.3826m.

111. The prudential indicators for Merseyside are

(a) Capital Expenditure

The actual capital expenditure that was incurred in 2008/09 and the estimates of capital expenditure to be incurred for the current and future years that are recommended for approval are:

	Actual 2008/09	**Estimate 2009/10**	**Estimate 2010/11**	**Estimate 2011/12**	**Estimate 2012/13**	**Estimate 2013/14**	**Estimate 2014/15**
	£000,s	**£000,s**	**£000,s**	**£000,s**	**£000,s**	**£000,s**	**£000,s**
Capital Expenditure	7,681	8,717	11,953	4,572	7,886	7,596	4,768

Members will note that the big rise in expenditure in 2010/11 reflects re-phased schemes from earlier years of approximately £7m (mainly around the building and vehicle programmes). The 2012/13 – 2013/14 figures include approximately £3.5m in each year for the fire world concept. More details on the capital programme are given elsewhere in the report.

(b) Ratio of financing costs to net revenue stream

Estimates of the ratio of financing costs to net revenue stream (amounts met from government grants and local taxpayers) for the current and future years, and the actual figures for 2008/09 are:

	Actual 2008/09	**Estimate 2009/10**	**Estimate 2010/11**	**Estimate 2011/12**	**Estimate 2012/13**	**Estimate 2013/14**	**Estimate 2014/15**
Ratio of Financing costs to Net Revenue Stream	**5.99%**	**6.24%**	**6.97%**	**7.50%**	**7.59%**	**7.67%**	**7.79%**

This shows that forecast debt financing costs will increase from 6.97% in 2010/11 (based on the actual forecast capital spend in 2009/10) to 7.79% (+0.82% points) by 2014/15.

(c) Effect on the Precept

The estimate of the incremental impact of capital investment decisions proposed in this budget report, over and above capital investment decisions that have been previously been taken by the Authority are:

	Actual 2008/09	**Estimate 2009/10**	**Estimate 2010/11**	**Estimate 2011/12**	**Estimate 2012/13**	**Estimate 2013/14**	**Estimate 2014/15**
	£	**£**	**£**	**£**	**£**	**£**	**£**
Incremental Impact of Capital Investment Decisions	**-0.36**	**-0.73**	**1.52**	-0.68	0.11	0.66	0.96

This indicator compares the capital programme set by the Authority in last year's budget process to the proposed revised capital programme submitted this year, and is intended to show the marginal impact of the overall capital programme new decisions being made by the Authority, on Council Tax levels. The re-phasing of expenditure from 2008/09, 2009/10 in to 2010/11 and the fire world from 2011/12 into 2012/13 has resulted in a negative or reduced incremental increase in some years.

Capital Financing Requirement

112. In accordance with best professional practice, the Authority does not associate borrowing with particular items or types of expenditure. The Authority has an integrated Treasury Management strategy (elsewhere on agenda) and has adopted the CIPFA *Code of Practice for Treasury Management in the Public Services*. The Authority has, at any point in time, a number of cashflows both positive and negative, and manages its Treasury position in terms of its borrowings and investments in accordance with its approved treasury management strategy and practices. In day to day cash management, no distinction can be made between revenue cash and capital cash. External borrowing arises as a consequence of all the financial transactions of the Authority and not simply those

arising from capital spending. In contrast, the capital financing requirement reflects the Authority's underlying need to borrow for a capital purpose.

113. Estimates of the end of year capital financing requirement for the Authority for the current and future years and the actual capital financing requirement at 31 March 2009 are:

	Actual 31.3.09	Estimate 31.3.10	Estimate 31.3.11	Estimate 31.3.12	Estimate 31.3.13	Estimate 31.3.14	Estimate 31.3.15
	£000,s	£000,s	£000,s	£000,s	£000,s	£000,s	£000,s
Capital Financing Requirement	**47,542**	**51,787**	**58,497**	**59,429**	**60,478**	**61,180**	**61,901**

Members will note that the capital financing requirement (CFR) is a "proxy" for debt outstanding.

The Authority's CFR is expected to increase to £61.9m by 2015 compared to current levels (end of 2008/09) of £47.5m. A large proportion of this increase was already anticipated in last year's programme (anticipated £59.6m by 2014).

Net Borrowing and the Capital Financing Requirement

114. CIPFA's *Prudential Code for Capital Finance in Local Authorities* includes the following as a key indicator of prudence:

"In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure that net external borrowing does not, except in the short term, exceed the total capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years."

115. The Authority had no difficulty meeting this requirement in 2008/09, nor are any difficulties envisaged for the current or future years. This view takes into account current commitments, existing plans, and the proposals in this budget report.

(F) TREASURY MANAGEMENT STRATEGY STATEMENT 2010/11

Introduction

116. This report sets out the expected treasury operations for this period, linked to the Authority's Medium Term Financial Plan, Financial Plan, Capital Strategy, Asset Management Plan and the Authority's Corporate Plan. It is inextricably linked to delivering the Authority's priorities and strategy. It contains three key legislative requirements:

(a) The Treasury Management Strategy Statement which sets out how the Authority manages its money through its treasury service to support capital expenditure decisions, day to day cash management and the limitations on activity through treasury prudential indicators. The key indicator is the Authorised Limit (the total of borrowing allowed) required by S3 of the Local Government Act 2003 and is in accordance with the (Chartered Institute of

Public Finance and Accountancy) CIPFA Codes of Practice.

(b) The reporting of the prudential indicators for external debt (as required by the CIPFA Prudential Code for Capital Finance in Local Authorities) and the treasury management prudential indicators (as required by the CIPFA Treasury Management Code of Practice). These indicators help assess the reasonableness and affordability of proposed borrowing.

(c) The investment strategy which sets out the Authority's criteria for choosing investment counterparties (a counterparty is an organisation we invest our money in) and limiting exposure to the risk of loss. This strategy is in accordance with the Communities and Local Government (CLG) Investment Guidance which was updated after issues arising from the Credit Crunch.

117. The Authority buys in Treasury Management Services from Liverpool City Council under a Service Level Agreement. Being a larger organisation Liverpool City Council is better placed to maintain a resilient up to date skills base to effectively deliver this complex technical service. The SLA dictates that the Treasury Manager at Liverpool must comply with this Authority Strategy. The system and process for Treasury Management and investments are reviewed by Audit.

118. Revised editions of the professional guidance on how to manage our investments and borrowing – the CIPFA Prudential Code and CIPFA Treasury Management Code of Practice - were produced in November 2009. The CLG is currently consulting on changes to the Investment Guidance. The revised guidance arising from these Codes has been incorporated within these reports, with the CLG proposals being incorporated where these do not conflict with current professional guidance. If necessary the Investment Strategy will be revised if any elements of the final CLG Investment Guidance have not already been covered.

119. The main changes initiated in the revised guidance are to increase the responsibility for Fire Authority Members in this area. This will require Members to scrutinise treasury policies, increased Member training in this risk critical area and awareness and the provision of more frequent detailed information. These changes have been introduced following high profile losses by Authorities in Icelandic Banks

120. One element of the revised CIPFA Treasury Management Code of Practice is that the clauses to be formally adopted as part of the Authority's Standing Orders and Financial Regulations must be amended to ensure they are explicitly reflected. This revision to standing orders and financial regulations are shown at Appendix 3 for approval. The key change is that the Performance and Audit Committee will be responsible for ensuring effective scrutiny of the treasury management strategy and policies, before making recommendations to Authority.

Summary

121. The above policies and parameters provide an approved framework within which the Officers undertake the day to day capital and treasury activities. The Authority is asked to consider each of the key elements contained within this section of the report:

(a) The Treasury Management Strategy 2010/11.

(b) The External Debt and Treasury Management Prudential Indicators and Limits for 2010/11 to 2012/13.

(c) The Investment Strategy 2010/11.

(d) A proposed revision to the Authority's Standing Orders and Financial Regulations at Appendix 3 to reflect latest CIPFA guidance. This revision nominates the Performance & Audit Committee to ensure effective scrutiny of the treasury management strategy and policies.

Treasury Management Strategy

122. The suggested strategy for 2010/11 in respect of treasury management is based upon Treasury Officers' views on interest rates supplemented by leading market forecasts. The strategy covers:

(a) prospects for interest rates;
(b) capital borrowing and debt rescheduling;
(c) annual investment strategy;
(d) external debt prudential indicators;
(e) treasury management prudential indicators.
(f) performance indicators;
(g) treasury management advisers

Prospects for Interest Rates

123. Short-term rates are expected to remain on hold for a considerable time. A recovery in the economy from recent turmoil is expected to be weak and protracted. Growth and inflation are set to remain subdued in the next few years and pressure on the MPC (Monetary Policy Committee) to raise the Bank Rate will remain moderate. However, some increase from the current 0.5% may be necessary in 2010/11 to counter the effects of external inflation pressure. This increase is not expected to be more than1.0% over the financial year 2010/11. (The MPC did not change interest rates on the 4th February).

124. Longer term rates are currently artificially low because of the effects of Bank of England intervention in the money markets. This may continue in the early part of 2010/11 but the process is likely to come to an end before the close of the financial year. The effect will be upward pressure on long term rates and longer-term Public Works Loans Board (PWLB) rates are expected to rise above 5% by the end of the

year. (On the 4th February the MPC stopped its policy known as quantitative easing).

125. The overall structure of interest rates is expected to remain the same with both short and long term rates increasing over the financial year. It is expected that short term rates will continue to be lower than long term rates and are likely to remain so throughout 2010/11. In light of this forecast, the proposed strategy will be to reduce investments and borrow for short periods and possibly at variable rates when required.

Capital Borrowings and the Borrowing Portfolio Strategy

126. The borrowing requirement comprises the expected movement in the Capital Financing Requirement (Broadly this is the amount required to fund the Authorities capital expenditure) and any maturing debt which will need to be re-financed. The Authority's net capital borrowing requirement for 2010/11 is presently estimated at £6.7m but this can vary if the capital programme is amended during the year. Given the likely structure of interest rates described above, it is envisaged that most of this borrowing will be for shorter periods or at variable rates. Against this background, Treasury Officers will monitor the interest rate market and adopt a pragmatic approach to any changing circumstances. This approach balances risk since most of the current debt portfolio has been borrowed at long term fixed rates.

127. Re-scheduling of debt is the early repayment of loans and replacement by loans for different periods and at different interest rates. It can be used to enhance the balance of the long term portfolio by for example amending the maturity profile or changing volatility levels and may on occasion generate cash savings. Debt rescheduling becomes more beneficial when the relationship between short and long term rates moves appreciably.

128. Some changes in the terms applied to PWLB (The Public Works Loan Board is the agency that the Fire Authority borrows from – its interest rates are nearer Bank of England base rates than commercial lending institutions) loans in November 2007 (i.e. the application of differing interest rates for borrowing and those for repayment) have severely constrained the option to generate savings via debt rescheduling. Under this regime, it will require a significant rise in the general level of interest rates to place debt in a position where rescheduling is viable. However, PWLB rules are being reviewed and easier terms for rescheduling may be introduced in 2010/11.

129. Interest rate structures will be continually monitored for opportunities to generate savings from debt rescheduling and in particular for opportunities to enhance the Authorities agreed strategy to maximise reserves in the short term as a buffer against future financial risks especially the likely pressure public sector grant funding will face. Any rescheduling that takes place will be reported to Members in monitoring reports.

Annual Investment Strategy

130. The purpose of the Annual Investment Strategy is to set out the policies for giving priority to the security and liquidity of the Authority's investments. The strategy deals with the credit ratings defined for each category of specified investments, the prudential use of non-specified investments, and the liquidity of investments. The investment strategy has regard to Government Guidance on Local Government Investments and CIPFA's Treasury Management in Public Services: Code of Practice and Cross Sectoral Guidance Notes.

131. The Authority's investment priorities are **(a) the security of capital** and (**b) liquidity of its investments.** The Authority will aim to achieve the optimum return on its investments commensurate with the proper levels of security and liquidity. All investments will be in sterling. All cash balances will be invested in accordance with the Code of Practice and with regard to the statutory guidance.

132. A counterparty list of institutions with which the Authority will invest shall be maintained by reference to the criteria set out below for the different categories of institution and their credit rating. Regardless of these criteria, the money market will be closely monitored and any institution will be suspended from the counterparty lending list should any doubts arise concerning its financial standing. Under the guidance investments fall into two separate categories, either specified or non-specified investments.

-Specified Investments

133. Specified investments offer high security and high liquidity and satisfy the conditions set out below:

- The investment is denominated in sterling and any payments or repayments in respect of the investment are payable in sterling only.
- The investment is not a long-term investment (has a maturity of less than one year).

- The investment does not involve the acquisition of share capital or loan capital in any body corporate.
- The investment is made with a body or in an investment scheme which has been awarded **a high credit rating** by a credit rating agency OR
- made with the UK Government or a local Authority or a parish or community Authority.

It is proposed that specified investments comprise the following institutions:

- UK local authorities
- Debt Management Account Deposit Facility
- Money Market Funds
- UK Banks, foreign banks registered in the UK and mutual building societies with a high credit rating

<u>-Credit Rating Criteria</u>

134. A high credit rating is interpreted as the Fitch Ratings Ltd criteria currently applied to the lending list. To be deemed highly rated the institution must satisfy at least the minimum of the following criteria:

- Long term credit rating A
- Short term credit rating F1
- Individual rating C

135. In addition, the Authority will use banks whose ratings fall below the criteria specified above if all of the following conditions are met (a) wholesale deposits in the bank are covered by a government guarantee; (b) the sovereign government providing the guarantee is rated “AAA” by all three major rating agencies (Fitch, Moody’s and Standard & Poors); and (c) the Authority’s investments with the bank are limited to amounts and maturities within the terms of the stipulated guarantee.

<u>- Investment Limits</u>

136. The credit ratings and individual limits for each institution within the categories of investments to be used by the Authority in 2009/10 are as follows:

UK local authorities	£3 million
Debt Management Account Deposit Facility	£3 million
Money Market Funds (AAA rated)	£3 million
UK Banks and Building Societies (AA or higher rated)	£2 million
UK Banks and Building Societies (A or higher rated)	£1 million
Foreign banks registered in the UK (AA or higher rated)	£1 million
Banks covered by Government Guarantee	£3 million

The maximum that may be invested with different banks that are part of the same conglomerate shall not exceed the maximum of the highest rated bank within the group. The limits may be exceeded for short periods when there are adverse conditions in the money market with the agreement of the Director of Resources or Treasury Manager.

137. Bank and Money Market Fund ratings are checked at least each month. The Authority is alerted by e-mail when there is an amendment by any of the agencies to the credit rating of an institution. If an amendment means an institution no longer meets the Authority’s minimum requirement or any doubt over its financial standing exists then that institution is removed immediately from the counterparty lending list. Conversely, an institution may be added to the list should it achieve the minimum rating.

- Non-specified investments

138. Non-specified investments do not, by definition, meet the requirements of a specified investment. The ODPM guidance requires that greater detail is provided of the intended use of non-specified investments due to greater potential risk. It is proposed that any cash balances invested in non-specified investments are undertaken only with mutual building societies that do not meet the specified criteria above.

139. The majority of building societies do not provide credit ratings to the credit rating agencies (so cannot be classed as specified investments) and inclusion on the lending list and individual lending limit has hitherto been determined by asset size. It is proposed to continue current practice and select the top ten building societies, determined by asset size, for inclusion on the counterparty list. Those societies that are within the top ten but do not have an agency determined credit rating shall have an individual limit of £1 million. Those that are credit rated will have limits determined by the criteria for specified investments. Building Society rankings are checked annually with the Building Societies Association.

- Liquidity of investments

140. Each investment decision is made with regard to cash flow requirements resulting in a range of maturity periods within the investment portfolio. All investments are normally short term having a maturity of less than one year. The Prudential Code does allow longer term investments and under certain money market conditions it may be prudent to invest for up to three years dependent on cash flow forecasts.

- Reporting Arrangements

141. The Investments Strategy forms part of the Treasury Management Strategy which is referred to Policy and Finance Committee for monitoring. Treasury Management activity is reported to Members during the year in the quarterly budget monitoring reports and in a final annual report by 30th September following the end of a financial year.

External Debt Prudential Indicators:

142. The Prudential Code requires the following external debt indicators of prudence:

- Authorised limit for external debt;
- Operational boundary for external debt

Authorised Limit

143. The Authorised Limit for Debt represents the maximum level of debt which the Authority may have during the year. The Authority has no powers to exceed this limit unless a further report with revised prudential indicators is approved by the full Authority. The limit therefore makes appropriate allowance for the risks and

uncertainties which affect day-to-day debt levels, and the ups and downs of short term cash flow.

144. The authorised limits reflect the Authority's capital financing requirements, identified in its capital expenditure and financing plans. They are consistent with treasury management policy statement and practices. The Authority is asked to approve the limits below and to delegate authority to the Executive Director of Resources, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities.

Authorised Limit for External Debt		**2010/11**	**2011/12**	**2012/13**
		£'000	**£'000**	**£'000**
Borrowing		63,000	64,000	65,000
Other Long Term Liabilities		2,000	2,000	2,000
TOTAL		**65,000**	**66,000**	**67,000**

Operational Boundary

145. The Operational Boundary is the expected maximum debt based on existing and forecast borrowings whilst the Authorised Limit has additional headroom for unexpected events that could lead to increased borrowing e.g. debt rescheduling could involve borrowing before repayment of debt.

146. The Operational Boundary indicator represents the expected maximum debt position during each year. It takes into account projections of borrowing requirement and repayments in future years. It may be different from the year end position as it reflects cash flows within each year. The Authority is asked to approve the limits and to delegate authority to the Executive Director of Resources, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities.

Operational Boundary for External Debt		**2010/11**	**2011/12**	**2012/13**
		£'000	**£'000**	**£'000**
Borrowing		53,000	54,000	55,000
Other Long Term Liabilities		2,000	2,000	2,000
TOTAL		**55,000**	**56,000**	**57,000**

Actual External Debt

147. The prudential indicator for actual external debt considers a single point in time and hence is only directly comparable to the authorised limit and operational boundary at that point in time. Actual external debt is monitored during the year against the limits. It is forecast to be £46 million at 31st March 2010.

TREASURY MANAGEMENT INDICATORS:

148. The Treasury Management Code requires the following Treasury Management indicators of prudence:

Upper limit on fixed interest rate exposures;

Upper limit on variable interest rate exposures;
Upper and lower limits for the maturity structure of borrowing;
Total principal sums invested for periods longer than 364 days.

Interest Rate Exposures

149. It is recommended that the Authority sets upper limits on its fixed and variable interest rate exposures as a percentage of its net outstanding principal sums as follows: -

Upper Limits on Interest Rate Exposures		**2010/11**	**2011/12**	**2012/13**
		%	**%**	**%**
Fixed		100	100	100
Variable		25	25	25

150. This means that the Executive Director of Resources will manage fixed interest rate exposures within the range 25% to 100% and variable interest rate exposures within the range 0% to 25% for 2010/11. A prudent strategy would expect there to be a mixture of fixed and variable rate loans (if for example all loans were at variable rate the risk of costs increasing significantly as interest rates change would be high)

Maturity Structure of Borrowing

151. It is recommended that the Authority sets upper and lower percentage limits for the maturity structure of its borrowings as follows. Percentage of projected fixed rate borrowing that is maturing in each period:

	Upper Limit	**Lower Limit**
Under 12 months	40%	0%
12 months and within 24 months	30%	0%
24 months and within 5 years	30%	0%
5 years and within 10 years	30%	0%
10 years and above	90%	0%

152. The reason for this control is so that not all debts mature (need replacing) at the same time because if they were there is risk that the point of time in question could be a disadvantageous one in terms of interest rates

Total Principal Sums Invested For Periods Longer Than 364 Days

153. It is recommended that the limit for investments of longer than 364 days be set at £2m for each of the years 2010/11, 2011/12 and 2012/13. The longer the term of an investment the more likelihood of conditions and risks changing across its life.

PERFORMANCE INDICATORS

154. The Code of Practice on Treasury Management requires the Authority to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the prudential indicators, which are predominantly forward looking.

155. The Authority will maintain performance indicators for both borrowing and investment though it must be stressed that the pursuit of higher performance shall not be at the expense of taking undue risks. The indicators for the treasury function are:

Borrowing - Average rate of borrowing for the year compared to average available. This tests if the borrowing achieved is at a competitive rate.

Investments – Internal returns compared to the 7 day LIBID rate. This tests the rate of return on investment being pro-actively managed compared to effectively a 'do nothing ' strategy . (*LIBID rate is the London Interbank Bid Rate. The 7 day LIBID rate is the benchmark used by local authorities for investment returns)*

The results of these indicators will be reported in the Treasury Management Monitoring and Annual Reports.

TREASURY MANAGEMENT ADVISERS

156. The treasury management service is provided to the Authority by Liverpool City Council. The terms of the service are set out in an agreed Service Level Agreement. The Council employs Treasury Management Advisers appointed under a competitive procurement exercise who provide a range of services which include:-

- Technical support on treasury matters, capital finance issues.
- Economic and interest rate analysis.
- Debt services which includes advice on the timing of borrowing.
- Debt rescheduling advice surrounding the existing portfolio.
- Generic investment advice on interest rates, timing and investment instruments.
- Credit ratings/market information service comprising the three main credit rating agencies.

157. Whilst Liverpool City Council and its advisers provide the treasury function, ultimate responsibility for any decision on treasury matters remains with the Authority.

(G) REVENUE FORECASTS

158. The Authority has in place a robust medium term financial plan.

This plan is fully reviewed on an annual basis and monitored quarterly. This section of the report will:-

- Firstly re-examine the underlying assumptions within the current financial plan.
- Discuss the changes that have occurred to that plan.

159. Members will recall that 4 years ago the Authority's budget forecasts had identified a deficit for 2006/2007 of £8.499m. If this deficit were to be covered by precept increases alone this would have required a precept increase in excess of 40%.

This had arisen because of:-

- Exceptional pensions expenditure in 2005/06 depleting reserves
- The Authority hoped that new funding arrangements for Firefighters pensions would eliminate the pensions problem altogether by returning expenditure to an "average" position. In fact the proposals, whilst stopping the problem getting any worse maintained the net revenue position at the 'exceptional' 2005/06 position. Therefore the Authority needed to repeat the one-off savings used to support the 2005/06 position.
- The significant imbalance between inflation and grant increases over a number of years.

160. Of this problem approximately £2.5m was one-off expenditure and the remaining £6m was a reflection of an underlying imbalance between income and expenditure levels. Of this £6m the 2006/07 plan assumed £5.2m would come from dynamic staff savings.

161. After the announcement of the CSR07 the Authority was allocated Government grant increases of +1.0%, +0.5% and +0.5% for 2008/09, 2009/10 and 2010/11, 4.5% below the level in the original 2006/07 financial plan. This reduction in funding resulted in the £5.2m dynamic staff saving target being increased by £2.4m and an overall target of £7.6m to be achieved by 2010/11. The Authority had of course made significant strides in addressing that underlying deficit and in the 2009/10 plan the Authority approved options to deliver the remaining savings:

Description	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
	£'000	£'000	£'000	£'000	£'000	£'000
Saving Options:						
Effectively Reducing ill health retirements	-200	-350	-350	-350	-350	-350
Review management Structures	-400	-400	-400	-400	-400	-400
Non Uniform Support Costs	-150	-150	-150	-150	-150	-150
Special Appliance provision/ORC	-280	-280	-280	-280	-280	-280
Grey Book/Green Book Review	-250	-250	-250	-250	-250	-250
Further Review of RRT (11 posts)	-400	-400	-400	-400	-400	-400
LLAR * 1	-300	-300	-300	-300	-300	-300
Apply Retirement Rengagement	0	-175	-175	-175	-175	-175
Income Generation through social enterprise	0	-175	-200	-225	-250	-250
Procurement Efficiencies Target	-200	-250	-250	-250	-250	-250
Self Rostering	-360	-360	-360	-360	-360	-360
Reduce R&R team to reflect riding appliances efficiently in line with agreements	-1,332	-1,332	-1,332	-1,332	-1,332	-1,332
Engineering Centre of Excellence	0	-150	-150	-150	-150	-150
Use of Cost Smoothing Reserve	283	-125	-392	-182	137	85
	-3,589	-4,697	-4,989	-4,804	-4,510	-4,562

The 2010/11 plan assumes the few remaining approved saving options to deliver the outstanding balance will be delivered as agreed:

Description	2010/11	2011/12	2012/13	2013/14	2014/15
	£'000	£'000	£'000	£'000	£'000
Saving Options:					
Engineering Centre of Excellence	-150	-150	-150	-150	-150
Apply Retirement Rengagement	-175	-175	-175	-175	-175
Income Generation through social enterprise	-175	-200	-225	-250	-250
Self Rostering	-360	-360	-360	-360	-360
Non Uniform Support Costs	-150	-150	-150	-150	-150
	-1,010	-1,035	-1,060	-1,085	-1,085

This means only variations to the approved plan need to be considered as part of this 2010/11 MTFP report.

Budget Assumptions

162. In compiling the plan, the Executive Director of Resources has, in consultation with the Chief Fire Officer, made a number of assumptions of both a technical nature and also about the policies that the Authority might be mindful to pursue in its aim for a Fire Safety Community.

Included within this underlying budget position are the following assumptions.

Inflation & Pay Changes

163. The forecast plan currently includes a contingency for pay awards and price increases in each year. This has been prepared using the following assumptions:

- Non Uniformed & Uniformed Pay – 2% annual pay award per year in line with Treasury expectations
- All Other Price Inflation - 2% p.a.

*What has changed?

(a) Pay

Members will recall that the Government has repeatedly emphasised the need in the current economic climate to manage public sector pay expectations… *"I can announce that, for the two years from 2011, we will seek to ensure that all public sector pay settlements be capped at 1%."* Alister Darling 09.12.09

This has been echoed by all political parties in statements on how they might address the public sector budget deficit.

(b) Pensions

An actuarial review of the firefighters pension scheme has been undertaken. The results of that review indicate that (all other things being equal) the increase in the cost of the scheme because of increased longevity would require an increase in employer's contribution of 3.1%. (The exact timing of any increase, any changes to the scheme and whether any element is payable by staff is yet to be determined by the Secretary of State)

In relation to the LGPS the Authority expects employer contributions to require increasing from 2011/12 following the next actuarial review of that scheme. The exact amount is difficult to forecast.

(c) National Insurance

The current financial plan anticipated an increase in employers NI of 0.5% from 2011/12. This has now been increased further by an additional 0.5%.

Conclusion

164. In light of all these uncertainties this financial plan has been amended to reflect the following revised assumptions:-

(i) A pay freeze for all staff in 2010/11 & 2011/12
(ii) A net increase in the total pay bill for 2010 – 12 of 4% in total to reflect increasing employer superannuation and NI costs
(iii) From 2012/13 staff pay awards are in line with HM Treasury long term inflation targets of 2%

165. The total inflationary provision for pay and price costs are approximately £1.6m per annum. (Any short-term savings on the overall pay and price provision will be credited to a reserve to help avoid compulsory redundancies if natural turnover rates can not deliver the required structural changes within the required timescale).

166. As an indicator to Members and a guide in assessing the volatility of inflation estimates - a movement of 1% in pay inflation equates to approximately £0.5m.

Cost of Capital Borrowing

167. The revenue impacts of capital investment decisions and the agreed 2010/11 – 2014/15 capital programme are included within forecasts. This includes new start schemes of £5.9m. The plan also takes into account the proposed MRP policy discussed previously in section D.

PFI

168. The Authority has been successful in winning PFI credits to make a massive investment in our building stock as part of leading a North West Fire & Rescue Services project. The anticipated contributions to lease costs arising from this have been built into budgets for future years at a net £0.550m (this compares to an approximate cost of a project funded by borrowing alone which would be at least £2m p.a.)

169. The Authority would require assistance to take forward a specialist scheme of this complexity in the fields of finance, law and property provision has been built into the financial plan for consultancy and MFRS costs over the PFI development period of £0.215m per year. Whilst the fees may seem large they are relatively low when compared to the forecast capital cost of the project (£45.4m).

170. Consultants working on the Project have identified that the Authority should consider maintaining a costs smoothing/affordability reserve for the PFI project to spread costs effectively and smoothly over the life of the project. This is common practice in such schemes. The level of this reserve will clearly need to be reviewed as the Project progresses and affordability gap becomes clearer but this action would leave the Authority well placed to deal with the financial burden of this innovative scheme. Any PFI funds remaining at the end of each year will be credited to the PFI reserve to provide an enhanced resilience against rising or unforeseen costs. **(Maintain the reserve at £0.695m)**

Resources Available

171.

(a) Council Tax /Precept

The position assumes council tax increases at the Authority's medium term planning level of 4.00% in 2010/11 and 4% per annum thereafter.

(b) Government Grant

Within the agreed plan assessed Government support reflects the already announced increases identified in Comprehensive Spending Review 2007 (CSR07), 0.5% increase in 2010/11. For future years (2011/12 onwards) an assumed increase in line with forecast inflation estimates of 2.0% p.a. Members will recognise that the unprecedented financial turmoil in recent months has put great pressures on the public purse and some commentators believe that grant settlements in 2011 and future years will be lower than this.

The Authority has already assumed for planning purposes only that it will be required to make savings of the order of £8m and the Budget Working Group has been considering this challenge.

Other Assumptions

172. The Medium Term Financial Plan assumes that:-

(a) Investment Income

The current financial plan assumes interest income from investments would deliver £0.100m in 2010/1 and £0.432m in future years. This was on the assumption that the adverse impact on interest rates caused by the recent economic climate (falling from +5% to less than 1% for new investments) would be reversed from 2011/12 .Uncertainty still remains over when interest rates will recover and therefore the proposed financial plan assumes investment income will be £0.050m lower than that currently assumed in 2011/12, but would then return to 2008/09 levels in future years.

(b) Regional Control and Firelink

The Authority has been told by the National project team that a NW regional control room will be operational by mid 2012. The final costs and business case remain unclear at this stage. Also it had originally been assumed that any cost increases arising from a new radio system to be implemented (Firelink) would be offset by efficiency savings arising from the joined up control room. In the 2009/10 – 2013/14 plan Members supported a request to be prudent and plan for an increase in costs of £0.5m from 2011/12 to cover both projects. This assumption has not altered.

(c) Regional Management Board £0.030m

Members will be aware that a number of successful projects have proceeded at Regional level. A provision of £0.030m, similar to previous years, has been built into the proposed financial plan to support regional working. This includes investment in the following work streams:

- Training
- Procurement
- Business Change Manager
- Administration and Audit Costs

(d) New Dimensions Grant

The Authority received a grant for 2009/10 & 2010/11 of £0.9m in each year for crewing New Dimensions vehicles from CLG. The financial plan assumes this grant will continue in 2011/12 – 2014/15.

Further Variations to the current Financial Plan

Increase in NI Rates

173. As a result of the announcement by the Government in the pre-budget report in December, 2009, that employers' national insurance will increase by a further 0.5% from 2010/11 (on top of the already announced +0.5%) a permanent increase of £0.250m p.a. has been built into the financial plan.

Impact of 2009/10 Pay Awards

174. The 2009/10 budget assumed pay awards for all staff would be 2%. However they came in below this at 1.25% for Firefighters and 1.00% for other staff, a permanent saving of £0.450m. This saving has been built into the latest plan.

Service Improvements £0.145m

175. Managers within the service were asked to identify potential areas for additional investment as part of the budget process. That initial process resulted in bids of over £1m. The Corporate Leadership Team has examined those bids in detail and restricted them to those areas which are unavoidable due to legislation or service improvement requirements. They total £0.143m in 2010/11 and £0.145m in future years. The table below details the growth requests built into the financial plan:

Description	2010/11	2011/12	2012/13	2013/14	2014/15
	£'000	£'000	£'000	£'000	£'000
CLT Growth					
Government review of business rateable values, +20% increase in NNDR.	50	75	75	75	75
2nd Internet Connection to improve community internet access	30	30	30	30	30
Vesty NNDR/Utility/Service Charge - (pending Derby Rd & Speke Workshop budget availability)	25	25	25	25	25
Firelink - Airwave insurance (10/11 only as £500k growth built in 11/12)	3	0	0	0	0
FSN Youth SLA ends 10/11. (CFS / FSN to cover post 10/11)	20	0	0	0	0
Fire Forum - Consultation Exercise	10	10	10	10	10
Marine 1 - (adjust overstated external contributions)	5	5	5	5	5
	143	145	145	145	145

Taxbase Collection Fund changes

Council Taxbase

176. The Districts of Merseyside have set their taxbases for 2009/10 and 2010/11 and they are shown in the table below:-

District	2009/2010 Council Tax Taxbase	2010/2011 Council Tax Taxbase	Variance	
	£	£	£	%
LIVERPOOL	126,626.00	125,359.00	-1,267.00	-1.0%
WIRRAL	104,276.00	104,690.00	414.00	0.4%
ST.HELENS	55,560.00	55,700.00	140.00	0.3%
SEFTON	92,946.68	93,050.25	103.57	0.1%
KNOWSLEY	42,031.00	41,862.00	-169.00	-0.4%
	421,439.68	420,661.25	-778.43	-0.2%
2009/10 Band D Tax Level	62.37	62.37		
Total Income £	26,285,193	26,236,642	-48,551	-0.2%

The total taxbase for the Authority has reduced by £778 (0.2%), this means that each £1 of Council Tax the level of income will be lower than that generated in 2009/10 by £778. The result of this is that the income from the current level of Council Tax is anticipated to reduce by £48,551 (this is assumed to be a permanent reduction).

This means that the income forecast from a 1% increase in Council Tax in 2010/2011 is now £262,366.

Surplus and Deficit on Collection Funds

177. The Districts of Merseyside have reviewed their collection funds and identified the proportion of any surplus or deficit attributable to the Authority. The results are set out in the table below and show a net deficit of £226,273. This impact is a one-off.

District	2009/2010 Coll fund deficit
	£
LIVERPOOL	169,000.00
WIRRAL	0.00
ST.HELENS	9,731.00
SEFTON	21,541.85
KNOWSLEY	26,000.00
	226,272.85

Grant Support

178. The 2010/11 increase has been confirmed at 0.5% but no announcement has been made for future years, in fact the Government has deferred the 2009 CSR until the summer of 2010. The current plan assumes grant increases at 2%, however the recent unprecedented economic position on public finances will impact on the availability of Government resources for grant settlements for this period.

179. Overall therefore the Fire Authority has a forecast underlying balanced budget position over the medium term.

180. This position may change if the underlying assumptions vary. The table below summarises the changes discussed in section G:

2010/11 - 2014/15 APPROVED FINANCIAL PLAN					
	2010/11	**2011/12**	**2012/13**	**2013/14**	**2014/15**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Approved Base Expenditure	73,767	76,055	77,926	79,754	82,019
Planned (Use) / Contribution to Cost Smoothing Reserve	-125	-392	-182	137	85
Approved 2009/10 5 Year Budget Financial Plan	73,642	75,663	77,744	79,891	82,104
Approved Amendments & Technical adjustments:					
Impact of lower 2009/10 pay awards	-450	-450	-450	-450	-450
Directors growth	143	145	145	145	145
Committee Approved Changes	0	53	53	15	15
Anticipated impact on Investment Income due to lower interest rates	0	50	0	0	0
Increase in NI rates by a further +0.5% from 2011/12 PBR		250	250	250	250
Ajustment to Planned (Use) / Contribution to Cost Smoothing Reserve	-9	-143	-96	-63	-67
Updated MTFP for 2010/11 Budget Report	73,326	75,568	77,646	79,788	81,997
Forecast Income					
Government Grant increase, +0.5% in 2010/11 then +2% thereafter	-46,304	-47,230	-48,175	-49,139	-50,122
Council Tax Increase assumed 4%	-27,336	-28,429	-29,566	-30,749	-31,979
Reduction in Council Tax Base	49	51	53	55	57
Collection fund deficit	226	0	0	0	0
Forecast Income in Financial Plan	-73,365	-75,608	-77,688	-79,833	-82,044
Forecast position (surplus) / deficit	-39	-40	-42	-45	-47

181. The service recognises significant uncertainty exists over some of the key assumptions within the plan. The suspension in announcing the next Comprehensive Spending Review has cast doubt over the level of government grant support beyond 2010/11. In light of the financial pressures facing the economy as a whole it is likely that government support will be reduced in future years. Other significant risks include:-

- The impact of the current economic climate;
- Inflation and future pay awards;
- Increases in the cost of public sector pensions;
- The future framework for local taxation and council taxes.

For planning purposes only the Service has adopted an efficiency target of £8m by 2015 over and above efficiencies in the current financial plan. Officers are commencing work with the Budget Working Group to begin exploring the options to deliver this efficiency.

(H) Future Consideration of Budget Options

182. Mindful of the potential future challenge, yet to be confirmed, this section of the report outlines the range of budget options identified by Officers in the 2009/10 plan but were not required to achieve the £5m saving target.

183. As Members will recall the Budget Working Group spent time developing a scorecard methodology so that all budget options could be scored against the Authority's key Value For Money Principles. Each of the options, 24 in total, was been scored using that methodology (see Appendix 4) and options were sorted in order of descending scores.

184. The 13 highest ranking options under this methodology (those scoring more than 30) were approved as part of the 2009/10 – 2013/14 financial plan.

185. The remaining 11 options are outlined below in rank order:

Option No	Option Title	Description	Saving £'000
24	Review the utilisation of second pumps and small fire units as a cohesive response to changed fire activity	A full review of the efffective utilisation of second pumps and small fires units can deliver efficiency savings and increased appropriate resources at high risk times	450
14	Change Shift patterns and vary support pump availability to match risk	This would mean changing contracts for all staff. By using overlapping shifts to vary reources according to risk significant cash savings could be delivered.	1,000
18	Remove 2 Fire Engines	Removing a single appliance on a risk basis -saves approximately £0.6m. Empirtical evidence from dispute that is possible	1,200
19	Remove 3 Fire Engines	Removing a single appliance on a risk basis -saves approximately £0.6m. Empirtical evidence from dispute that is possible	1,800
20	Close 1 Single Pump Fire Station	Removing a one pump fire station saves approximately £1m. A 2 pump twice that. Empirical evidence from dispute that is possible	1,000
21	Close 1 Two Pump Fire Station	Removing a one pump fire station saves approximately £1m. A 2 pump twice that. Empirical evidence from dispute that is possible	2,000
23	Reduce Response standards to national norm	Initially at least 3 stations retained. Longer term rationalise number of fire stations	2,000
15	Change Annual leave Allocation	By being more prescriptive about staff leave we can reduce staffing models and save costs. Staff will not be able to get leave as easily at the times they want	300
16	Extend agreed retained Resilience at one station	Retained reilience duty system has been used effectively at Bootle Netherton and Bromborough. Staff are paid addition retained fees for providing cover overnight that si called in on a resilience basis as risk across then county changes	250
17	Remove 1 Fire Engines	Removing a single appliance on a risk basis -saves approximately £0.6m. Empirtical evidence from dispute that is possible	600
22	Outsource Aspects of the Service	Private sector may take more ruthless approach to staffing efficiency through redundancy. This is offset by profit margin. Some local authorities have delivered efficencies by outsourcing processes and sharing costs across authorities	????
			10,600

186. The Authority has for many years now had an embedded strategy for VFM. The Authority has recently reviewed that strategy and reaffirmed its value for money principles (CFO/52/09). As stated already the above options adhere to these principles and take into account the aims in the Authority's mission statement. These may be summarised as:-

Value for Money Principles

Our Mission is:

To work in partnership to provide an excellent, affordable service to all the diverse communities of Merseyside that will:

•***Reduce*** *risk throughout the community by protective community safety services.*

•***Respond*** *quickly to emergencies with skilful staff who reflect all the diverse communities we serve.*

•***Restore,*** *maintain and improve the quality of life in our communities.*

•***Organisation,*** *ensure that our organisation provides quality value for money services*

Our Value for Money Principles express the outcomes we aim to achieve from our strategy and are:-

Principle 1 – Allocate resources In line with priorities

Principle 2 – Control Council Tax

Principle 3 – Acknowledging budget realities

The Authority will continue to:

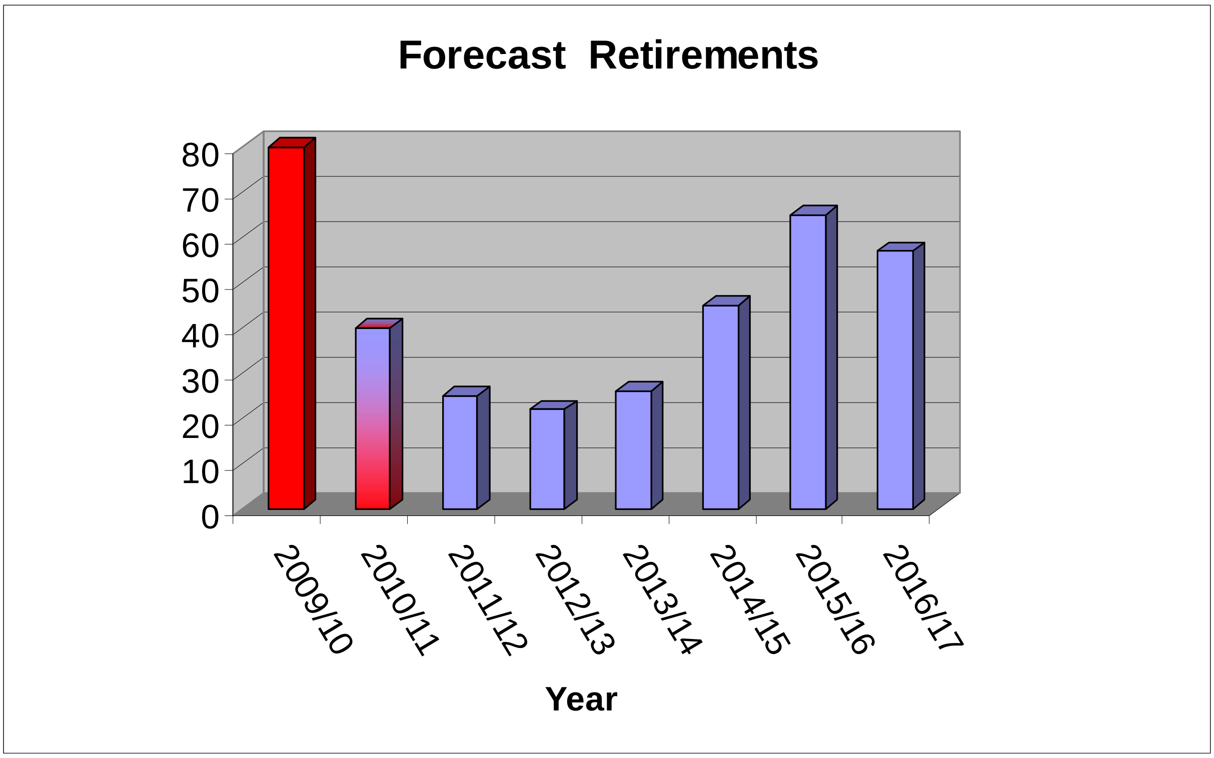
(i) Acknowledge the challenges it faces:
(ii) Acknowledge the reality of its budget and recognise that 80% of its costs are people related.

Principle 4 – The Authority seeks to avoid compulsory redundancy in delivering VfM

Principle 5 - The Authority seeks to maintain or improve service levels to make Merseyside safer, stronger, healthier

Deliverability of any Additional Saving Options (above and beyond current plan) and avoiding Compulsory Redundancy

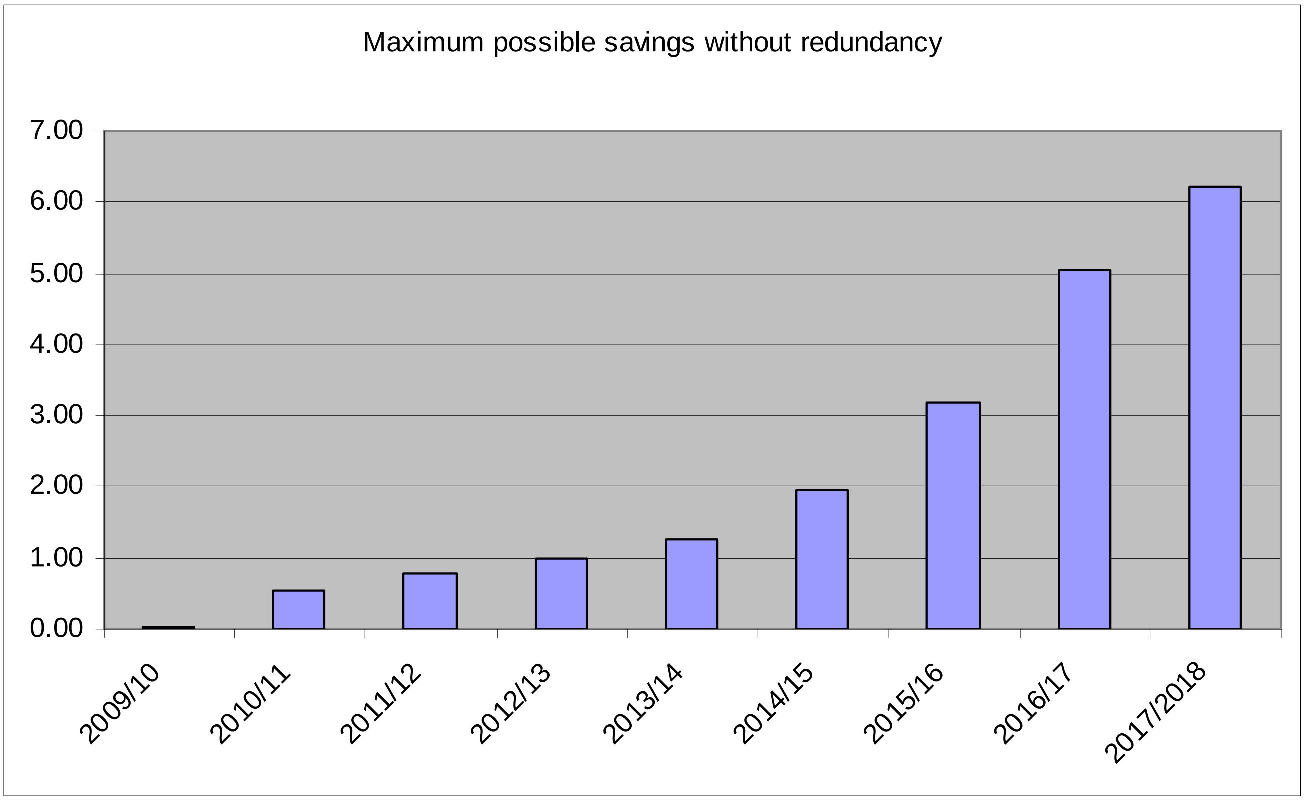
187. If the Authority is to avoid compulsory redundancy it must use natural turnover rates to reduce staff numbers. Key to this approach is the rate of Firefighter retirements. Anticipated retirements are set out in the chart below:-



Members will note that:

(a) retirement numbers are high in the early years giving scope for significant savings;
(b) the retirement savings up to 2010/11 are committed to the current financial plan saving target;
(c) that the opportunity for savings beyond 2010/11, at least in the initial three years is very limited as retirements reduce to about 20 per year from 2011/12.

188. The Executive Director of Resources has estimated the maximum possible cash saving that may be delivered by using natural turnover rates (including non-uniform turnover and allowing for one recruit course of 16 Firefighters per annum). This is set out in the table overleaf.



On the basis of these forecasts it is considered that compulsory redundancy can be avoided in relation to the current financial plan and the known £5m saving target.

<u>IF</u> any of the key assumptions in the current plan around future pay, grant, pension and tax increases is subject to an amendment then the Authority's ability to deliver savings over the 2011/12 – 2013/14 period through retirement rates is limited.

Council Tax/Precept

189. Members will have to decide their strategy for the precept and consider the acceptability of precept increases over the next few years.

Council Tax Capping

190. Universal crude capping of Council Tax has been abolished. However, new reserve powers have been introduced in the Local Government Act 1999 that allow the Secretary of State to intervene in certain instances.

191. The Government has said that keeping council tax under control remains a high priority for the Government and it expects the average increase in England to be below the 2009/10 3% average increase in local authorities next year.

192. It is clear that authorities setting high council taxes might well face capping, the Government has said it will not hesitate to use its capping powers as necessary to protect council tax payers from excessive increases. The Government has used its powers in recent years and capped a number of Authorities. The cost of 'rebilling' in the five Districts of Merseyside should the Authority be capped is estimated at £2m.

193. The 'ready reckoners' below will give Members a guide on the impact of various precept levels

Council Tax Increase

	0%	1%	3.85%	4%	5%
Band D Tax	62.37	62.99	64.77	64.86	65.49
District Precept	£m	£m	£m	£m	£m
LIVERPOOL	7.819	7.896	8.120	8.131	8.210
WIRRAL	6.530	6.594	6.781	6.790	6.856
ST.HELENS	3.474	3.509	3.608	3.613	3.648
SEFTON	5.804	5.861	6.027	6.035	6.094
KNOWSLEY	2.611	2.637	2.711	2.715	2.742
	26.238	26.497	27.247	27.284	27.550

194. The agreed medium term financial plan assumes a council tax increase of 4%. If Members agree an increase at this level it is likely that it will be relatively high compared to most other fire authorities (and local authorities)

195. In light of the Government comments there exists the possibility that this level of council tax increase might be capped.

196. However in light of:

- the poor grant increase of 0.5%
- a declining tax base and collection fund deficit
- the strategic approach to avoiding compulsory redundancy
- the low overall budget total increase of 1.7%

- a strategic approach over 6 years that has controlled council tax at a 4% average over all that period
- a below average council tax level
- good medium term performance controlling council tax

It is unlikely (although not impossible) that such a level might be capped

If the council tax was capped the cost of re-billing the five districts of Merseyside is estimated at £2m. Additional savings (probably by compulsory redundancy) would have to be found.

(I) ADEQUACY OF RESERVES AND BALANCES

Responsibilities of Chief Finance Officers

197. Under Part 2 of the Local Government Act 2003, the Chief Finance Officer of an Authority is now required to comment on the following matters:

    (a) the robustness of the estimates made for the purposes of determining its budget requirement for the forthcoming year;

    (b) the adequacy of the proposed financial reserves.

198. There is then a requirement for the Authority to have regard to the report of the Chief Finance Officer when making decisions on its budget requirement and level of financial reserves.

199. In the Fire Authority the Chief Finance Officer is the Executive Director of Resources – Kieran Timmins. For the purposes of the Act the “financial reserves” of the Authority would incorporate Earmarked Reserves and Working Balances.

200. To make a final judgement on these issues it will be necessary to consider the proposed budget decisions of the Authority in the light of this budget report.

Robustness of Estimate

201. To fully satisfy the Chief Finance Officer any proposed Budget or amendment should therefore:

    - Be fully based upon the advice of Service Officers (supported by finance officers) – or based upon or supported by information the Chief Finance Officer considers reasonable to accept.

    - Provide only for budget proposals that are fully costed to service level and where the implications – both financial and upon service performance – are estimated and identified.

    - Provide for all known future developments either through direct service budget allocations or the establishment of specific reserves for such purposes.

- Provide for an adequate level of Balances and Reserves consistent with the requirements of any regulation that may be earmarked and/or the Authority's own risk assessment.

- Provide for the full revenue implications of the Capital Programme.

- Establish clear targets for income collection in respect of key income streams.

- Ensure there are no unidentified savings targets.

- Where appropriate ensure that the consequences of current over and under spendings have been taken into account.

<u>Adequacy of proposed Financial Reserves</u>

202. Under the 2003 Local Government Act the Secretary of State may enact regulations that define certain types of "controlled reserves" and the minimum level for those reserves. At the time of preparing this report the Secretary of State has not enacted any such regulations.

203. However, the 2003 Act still places a requirement upon the Chief Finance Officer to report if the level of reserves is likely to be inadequate. That report should contain comment upon:

- the reasons for that situation
- the actions if any, considered appropriate to prevent the situation arising.

204. There is then a requirement for the Authority to respond to the report when making decisions on its future financial reserves.

205. In recent years the Authority has maintained a general revenue reserve of £2m and also maintained a number of earmarked reserves.

206. A pilot Comprehensive Performance Assessment (CPA) performance indicator relating to Financial Reserves indicated that an appropriate level of General Fund Working Balances at the end of the financial year should be "at least equal to 5%.... of forecast Net Operating Expenditure…. or there is a financial risk management process operating which the Authority uses to justify a lower level of reserves….". This is for 'normal', multi-service local authority.

207. For the Authority 5% forecast Net Operating Expenditure equates to approximately £3.5 million.

However:-

(b) The Authority's risk management arrangements have improved. As part of this budget process the Executive Director of Resources has prepared *a financial risk management matrix* and also assessed the year on year variation in risk facing the Authority. This takes account of the Corporate Risk Register.

(c) The Authority has previously maintained a number of specific earmarked reserves against risk.

(d) The Authority is single purpose and does not face as full a range of risks to manage as a multi-purpose authority.

(e) The Authority is unlikely to face significant increases in cost because of uncontrollable demand issues (unlike for example Social Services care for the elderly).

(f) Members will note that the Authority's revenue reserves have not generally been consumed during the year by overspendings but have been maintained throughout the year.

208. Having reviewed the Authority Risk Register and prepared a detailed costing of financial risks, the Executive Director of Resources recommends that in the light of all risks facing the Authority that it should aim to maintain a general revenue reserve of at least the current level of £2.5m.

209. It should, however, be noted that the as part of the risk assessment process four potential major risks have been identified for future years of the financial plan these are set out in the table below:-

RISK / ASSUMPTION	WHAT IF DIFFERENT
Pay awards **Inflation is on the increase and staff aspirations for pay awards over the 2010 – 2015 period may be greater than that assumed in future years. 2010/11 & 2011/12 assume a pay freeze**	**Each 1% variance changes budgets by £0.5m**
Grant Increases at 2% 2011/12 onwards **Many commentators believe public services may see a cash freeze or even reduction in the next spending review period as public sector finances face a challenging time following the recent economic turmoil.**	**A cash freeze in grants equates to £1m p.a. approx**
Council Tax Increased at 4% **Government have indicated the expectation the increases should be lower than the 2009/10 average of 3%. Some of the political parties are committed to freezing council tax levels if they are elected in a general election.**	**A freeze of council tax levels is equivalent to lost income of £1m p.a. approx**

<u>Pensions</u> **The financial plan assumes any cost changes can be contained within the overall pay provision increases of 4%.** **A Government Actuarial Department (GAD) review has identified employers costs should (if that is the only change) increase by 3.1% for the firefighter scheme.**	**It is currently unclear how the cost might be split between employer / employee / government or if the scheme might be charged and the timing of changes** **A 1% variation in employers contributions is £0.5m p.m.**

210. Clearly if any of these risks are realised then there will be significant permanent changes in the financial plan and the Authority would have to make permanent savings to balance its budget. As discussed in the budget options section of the report the scope for making additional further savings beyond the deficit identified without compulsory redundancy in the medium term is more limited because beyond 2011/12 the number of retirements reduces significantly for a three year period. Numbers of retirements increase again after 2014/15 to about 60 in a year.

211. The Executive Director of Resources believes that the Authority should aim to maintain and increase reserves over the next few years so that it has some resources available to use as part of a medium term financial strategy should any of the above risks be realised. This would allow it to balance the budget in the short term and give it more time to make permanent longer term savings and avoid comprising its value for money principle of compulsory redundancy.

212. To that end the Authority already has :-

A Modernisation Reserve	£581,000
A Costs Smoothing reserve	£2,391,000
An Inflation Reserve	£858,000

As far as possible the Authority should seek to maintain those reserves until the position on the key risks becomes clearer and the medium to longer term financial plan has more certainty.

213. The currently forecast position on anticipated reserves is set out below:-

	31.03.10	31.03.11	31.03.12	31.03.13	31.03.14	31.03.15
	£'000	£'000	£'000	£'000	£'000	£'000
SPATE / Other Emergencies						
Bellwin Reserve	**147**	147	147	147	147	147
Insurance Reserve	**220**	220	220	220	220	220
Emergency planning	**75**	75	75	75	75	75
Modernisation Challenge						
Modernisation Reserve	**581**	581	581	581	581	581
Smoothing Reserve	**2,391**	2,257	1,722	1,444	1,518	1,536
Capital Investment						
PFI/Capital Reserve	**695**	695	695	695	695	695
Capital expenditure Reserve	**8**					
TDA Refurbishment Reserve	**68**					
Specific Projects						
Job Evaluation Reserve	**430**					
Regional Reserve	**100**	100	100	100	100	100
Information Systems Reserve	**60**					
Contestable Research Fund	**15**					
Equipment Reserve	**30**					
Training Reserve	**195**	195	195	195	195	195
Pre Retirement reserve	**143**					
FSN Reserve	**0**					
FSD Reserve	**0**					
Healthy Living/Olympic Legacy	**260**					
Inflation						
Inflation Reserve	**858**	858	858	858	858	858
Ringfenced Reserves						
F.R.E.E. Reserve	**17**					
Princes Trust Reserve	**113**					
Community Youth Team	**43**					
Beacon Peer Project Reserve	**165**					
Innovation Fund Reserve	**148**					
Concept Knowsley	**18**					
Regional Control Reserve	**177**					
Energy Reseve	**66**					
St Helens District Reserve	**0**					
New Dimensions Reserve	**75**					
Total Earmarked Reserves	**7,098**	5,128	4,593	4,315	4,389	4,407
General revenue Reserve	**2,543**	2,543	2,543	2,543	2,543	2,543
Total reserves	**9,641**	**7,671**	**7,136**	**6,858**	**6,932**	**6,950**

Members will note in particular regarding the reserves

214. The modernisation reserve was set up following savings identified by changing accounting policies on smoke alarms. It is intended for use for one off costs that deliver long term savings. Notably paying for Service investment and VER/VS costs associated with the modernisation of the service required to deliver long term efficiencies. It is expected that a significant portion of this reserve will be used over the next year or two. At this stage the use of the reserve is not built into the above

forecast. Any proposed use of the reserve to fund VER/VS costs will be reported to Members.

- Smoothing reserve to provide a contingency for the delay between implementing the proposals to deliver the required savings and any shortfall in cash savings from retirements and other staff savings
- Inflation reserve to provide a one-off resource if inflation or pay varies from the assumptions in the plan
- The Authority hold a few other small earmarked reserves for specific purposes/potential costs – Bellwin Scheme, Insurance, Regional Efficiency and Emergency Planning.

Members should bear in mind that reserves and balances should only be used to finance one-off expenditure. If such monies are used to fund ongoing revenue expenditure without taking action to reduce underlying expenditure, the Authority would find itself facing the same deficit in the next and future years but without reserves available to finance it. This is underlined by the District Auditor's 'Golden Rule' - that "one off" revenue reserves should not be used to support 'ongoing' revenue expenditure.

Review of Reserves and Balances

215. Members need to consider their strategy on reserves and balances in the light of the guidance from the Executive Director of Resources.

Consultation

216. The Authority has consulted on its budget decision in a variety of ways and in particular:-.

(a) IRMP Consultation

As part of the IRMP consultation, some respondents commented on the level of Council Tax. The key message was that – whilst recognising that planning for 4% might seem reasonable, this is still twice the rate of inflation and will cause problems for pensioners and those on low incomes.

(b) Consultation with Unions/Staff

Trade Unions were invited to, and attended, the recent budget seminar and contributed to the debate around suitable options.

Budget Timetable

217. There is a legal requirement for the Authority to set a balanced budget and decide its level of precept **before** 1st March 2010.

Equality & Diversity Implications

218. The financial plan makes the required investment to ensure the Authority meets and exceeds its equality and diversity requirements in addition to work carried out by all staff and teams.

Health & Safety and Environmental Implications

219. The budget and capital investment programme make largescale investments in staff health and safety

Financial Implications & Value for Money

220. As contained within the report.

Contribution to Achieving the Vision:
"To Make Merseyside a Safer, Stronger, Healthier Community"

221. Sound budgetary management and the delivery of services within the approved budget helps the Authority deliver on its corporate aim of operating efficient and effective organisational functions that will support the core functions of the Authority in a way that provides value for money for the communities of Merseyside.

BACKGROUND PAPERS

Report CFO/021/09 "Merseyside Fire & Rescue Authority Budget & Financial Plan 2009/2010 – 2013/2014" Authority 26 February 2009.

Report CFO/012/10 "Financial Review Report 2009/10 April to December Review" Authority 18 February 2010

Glossary

CFR – **Capital Financing Requirement** – measures the amount of capital spending that has not yet been financed by capital receipts, capital grants or contributions from revenue income. It measures the underlying need to borrow for capital purpose, although this borrowing may not necessarily take place externally (use of available cash etc).

CFS – Community Fire Safety

CSR07 – Government comprehensive spending review to identify support for the public sector over 2 to 3 year period

HFSC – Home Fire Safety Check

LLAR – Low Level Activity Risk

MRP - MINIMUM REVENUE PROVISION - An amount set aside from revenue towards the repayment of loan debt.

MTFP – Medium Term Financial Plan

PFI - PRIVATE FINANCE INITIATIVE – a central government initiative which aims to increase the level of funding available for public services by attracting private sources of finance. The PFI is supported by a number of incentives to encourage authorities' participation.

RESERVES -Amounts set aside to meet future contingencies but whose use does not affect the Authority's net expenditure in a given year. Appropriations to and from reserves may not be made directly from the revenue account.

RSG – Government grant support towards the revenue budget

Supported Borrowing – Borrowing to fund capital expenditure that through the Revenue Support Grant receives grant support to cover the revenue costs associated with borrowing (interest / debt repayment)

Unsupported Borrowing – No Revenue Support Grant to cover the costs associated with borrowing and the Authority must earmark revenue funds to cover these costs.