AGENDA ITEM: 9

REPORT TO:	MERSEYSIDE FIRE & RESCUE AUTHORITY BUDGET AUTHORITY MEETING
DATE:	26TH FEBRUARY, 2013
REPORT NO.	CFO/025/13
REPORTING OFFICER:	DEPUTY CHIEF EXECUTIVE
CONTACT OFFICER:	DEPUTY CHIEF EXECUTIVE
OFFICERS CONSULTED:	STRATEGIC MANAGEMENT GROUP

Merseyside Fire and Rescue Authority Budget and Financial Plan 2013/2014- 2017/2018

Merseyside FIRE & RESCUE SERVICE

Beacon Authority 2004-2005 Services for Older People

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

Beacon Authority 2008-2009 Reducing Health Inequalities

APPENDIX	**1 (A) & 1 (B)**	**DRAFT REVENUE BUDGET ANALYSIS**
APPENDIX	**2**	**PROPOSED CAPITAL PROGRAMME 2013/14 – 2017/18 SUMMARY**
APPENDIX	**2A**	**CURRENT APPROVED CAPITAL PROGRAMME 2012/13 – 2016/17**
APPENDIX	**2B**	**PROPOSED NEW CAPITAL SCHEMES 2013/14 – 2017/18**

ATTACHED – HARD COPIES
***A Glossary of Terms has been listed at the end of this report for your information.**

<u>Purpose of Report</u>

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 2013/2014 and a precept level in line with statutory requirements.

<u>Recommendation</u>

2. Members consider this report and proposed budget 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 2013/2014 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 2013/2014 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) Approve the statement within this report that sets out the Authority's policy on the Minimum Revenue Payment (MRP) for 2013/14.

Introduction & Background

Information

3. The Authority is required to determine its budget and precept level for 2013/2014 by 1st March 2013.

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	Page
A	Executive Summary	3-10
B	Background Information	11-22
C	Capital Programme	23-29
D	Minimum Revenue Provision Statement	30-32
E	Prudential Indicators	33-35
F	Treasury Management Strategy	36-44
G	Revenue Forecasts 2013/14 – 2017/2018	45-52
H	Options for Tackling the Financial Challenge	53-58
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A) EXECUTIVE SUMMARY

7. The Authority must set a balanced budget and a precept level by 1st March 2013.

8. The budget and financial plan should allocate resources in line with the Authority's Mission and aims:-

Our Mission:

To Achieve; Safer, Stronger Communities - Safe Effective Firefighters

Our Aims:

Excellent Operational Preparedness
Excellent Operational Response
Excellent Prevention and Protection
Excellent People

9. The Authority has agreed a number of Value For Money Principles that have underpinned its approach to budgets and financial plans in recent years. During 2012/13 the principles were reviewed and updated to better reflect the challenges facing the Authority now and in the future. They are:-

Principle 1 – Allocate resources in a way that contributes towards the achievement of MFRA's Mission, Aims and Values

Principle 2 – To continue to seek to avoid compulsory redundancy (if possible given the difficult financial circumstances)

Principle 3 – To choose budget options which minimises negative impact on the front line services or on firefighter safety

Principle 4 – To consider budget approaches which ensure the right balance between local and national funding levels and considers the views of local people on the right level of council tax balanced against aspirations for service levels

Principle 5 – To allocate resources having considered the impact on our diverse communities and our employees.

Revenue Forecasts

10. As Members are aware the Authority is facing an unprecedented financial challenge over the 2011/2012 – 2014/2015 period.

11. Over the 2011/12 to 2012/13 period the Authority received the worst grant cuts for any fire authority in the country from central government, a cumulative reduction of in excess of 13%.As a result the Authority approved a saving plan for this period that balanced the budget for these years by making cuts and savings totalling £9.2m.

12. The Government has now announced the "formula" grant settlement for 2013/14 and given an indicative settlement figure for 2014/15. MFRA's grant cut is 8.7% and 7.5% respectively this is equivalent to a £6.3m cash cut. MFRA's grant reduction is worse than the national average for fire and rescue services grant cuts of 7.5% and 7.5%.

13. A draft forecast has been prepared using the balanced budget for 2012/13 as a starting point. This has been adjusted to take into account the latest grant settlement figures, and the following key assumptions:

- An increase in council tax by 2% in 2013/14 and 2% in 2014/15 (on the basis this will be the maximum allowed by the Government) and thereafter to keep to its medium term plan and have the freedom to set Council Tax at 4% per annum

- A paybill increase of 2% for all staff in line with the Treasury medium term inflation targets of 2% per annum (Pay bill includes such costs as pay awards, pension contributions and national insurance.)
- 2% per annum General Price Inflation
- Allowances for the variation in capital financing costs

A five year financial revenue estimate has been prepared based upon the current approved financial plan this identifies a deficit £10m over the 2013/14 – 2014/15 (Phase 2) period. Table A below summarises the financial position:-

Table A

2013/14 - 2017/18 FINANCIAL PLAN					
	2013/14	**2014/15**	**2015/16**	**2016/17**	**2017/18**
	£'000	**£'000**	£'000	£'000	£'000
NET EXPENDITURE:					
2013/2014 Financial Plan	**71,846**	**74,410**	**76,265**	**78,075**	**79,775**
FUNDING					
Government Funding					
RSG Grant	-22,194	-18,900	-17,790	-16,681	-17,014
Business Rates:					
Local Business Rate Share	-4,069	-4,194	-4,278	-4,363	-4,451
Top Up Grant	-10,696	-11,111	-11,333	-11,560	-11,791
Formula Funding Grant settlement	-36,959	-34,205	-33,401	-32,604	-33,256
Council Tax Support Grant	-6,392	-6,392	-6,200	-6,018	-6,087
2011/12 Ctax Freeze Grant	-681	-681			
Start-Up Allocation; Government & Business Rates Funding	-44,032	-41,278	-39,601	-38,622	-39,343
Business Rates: Increase in local forecast	-15				
Council Tax -					
2012/13 Revised base	-22,176	-22,619	-23,072	-23,995	-24,955
Assume 2% rise 2013/14 & 2014/15, 4% therefafter	-443	-453	-923	-960	-998
Collection Fund (surplus)/deficit	-55				
Forecast Council Tax Income	-22,674	-23,072	-23,995	-24,955	-25,953
Updated Income Forecast	**-66,721**	**-64,350**	**-63,596**	**-63,577**	**-65,296**
Forecast Net Position (surplus) / deficit	**5,125**	**10,060**	**12,669**	**14,498**	**14,479**

The revenue position is considered in more detail in section G.

14. Members should note that whilst no detailed figures have been announced the government has indicated that it is likely that reduction in public spending might well continue until 2017 and that Authorities might assume that these cuts would follow a straight line trajectory from those already enacted. The forecast reflects some assumptions around this approach and would indicate that, if confirmed, the forecast deficit might increase by a further £4-5m in 2016/17 and 2017/18.

Budget Options

15. The Authority recognised that these challenges were likely and last year commissioned a number of reviews and work programmes to identify savings. A complete review of Back office and Support areas (many of the areas in this review in fact provide front line services but are not operational response) has identified £7m worth of savings as set out in the table overleaf (a fuller report on this work appears elsewhere on the agenda) :-

No	Option	£'m
1	**Overachieved Savings** The Authority has overachieved in savings delivery of its Phase one plan against a £9.2m total saving target. Members might utilise that saving to support the financial plan	0.670
2	**Pay Bill Assumptions** The forecast contains an assumption that the total paybill increase will be 2% per annum. Members may take a view that it is likely that there will be further pay restraint for staff for the next two years in light of Government assumptions and comments from Treasury Ministers. Assuming a further two years of pay restraint for all staff and reducing the provision for pay bill increase to 1%- saving £1.0million. There are significant risks associated with this approach (even at a 2% level) and the DCE recommends holding specific reserves for the short term to cover any pay increases higher than this recognising that in the medium term yet more savings will be required if this is the case. Pay bill includes employer pension contributions and national insurance contributions that may also vary.	1.000
3	**Review of Inflation provision** The DCE has reviewed the baseline provision for inflation in the financial plan to reflect the 'downsizing' of the budget which means many budgets can be cash limited as volumes of expenditure reduce. The cumulative impact of this applied over several years is significant	£1.500
4	**Review of Capital Programme** Taking account of the capital grant received from government, re-phasing of the capital programme, reviewing investment income, the ability to restructure debt and reviewing asset expenditure profiles down to reflect the likely future position of the service has allowed the DCE to identify savings in the capital programme revenue costs	£1.000
5	**Income Generation** Officers have reviewed in detail the opportunities for generating extra income from service areas and have identified an additional £0.5m in total from:- a) PFI Fire station use by the ambulance service b) Increased efficiency through the JCC c) Shared services at the vehicle workshops d) Cost recovery of smoke alarms from low risk households	£0.500

6.	**Review of Support Services** A fundamental review of all support services has been undertaken and is reported elsewhere on the agenda.(CFO/026/13). It should be noted that this puts at least 57 non-uniform posts at risk of redundancy and that many of the "support service" areas and posts affected in fact provide front line services to the community of Merseyside notably prevention and protection	£2.307
7	**Members Allowances** Members have already committed to reducing the overall cost of members allowances by 10%	£0.020

16. Despite the significant savings identified this still means that £3m savings are required from operational response. A review of operational response also appears elsewhere on this agenda and it identifies how savings of £3m can be delivered. This translates to a reduction of 90 fire-fighter posts and a 33% cut in the number of appliances available from the beginning of the spending review from 42 to 28.

Reserves and Balances

17. In the light of the financial risks facing the Authority the Deputy Chief Executive has worked with Officers and Members to increase reserves in recent years. The latest financial review report CFO/024/13 identifies a forecast revenue underspend which will allow the Authority to increase its reserves by a further £2.5m meaning approximately £14.9m of reserves might be seen as available. Whist these levels are relatively high historically, they reflect the very high level of risk associated with the current financial plan and the severity of cuts imposed on the Authority in phase 2 and potential beyond 2014/15. The Authority needs a buffer to give it time to make changes if required and to avoid compulsory redundancy if possible

18. Based upon assumptions that the Authority will adopt all the savings identified and their attendant risks the Deputy Chief Executive recommends the Authority hold the following reserves at the start of the financial plan:-

	£'m
Insurance / Catastrophe Reserve	1.0
Inflation / Pension Reserve	1.5
Capital Reserve	2.0
Cost Smoothing Reserve	5.5
Recruitment Reserve	1.0
Severance Reserve	1.0
Total	12.0
General Fund	2.9

19. 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.

20. 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

21. The forecast produced assumes a 2.00% council tax increase in 2013/14 and 2014/15 and then 4.00% in each year in line with the Authority's value for money principles.

22. The Authority may choose to use a further precept increase to bridge the gap, however current legislation requires any increase above a threshold set by the Secretary of State must be subject to a referendum of the electorate of Merseyside. Any vote against such an increase will require a revised budget and incur the expense of re-billing all the districts within Merseyside. For 2013/14 any proposed increase in excess of 2% will require such a referendum.

23. Alternatively the Authority might take-up the option of the council tax freeze grant in 2013/14, (this would be payable for 2 years and would be equivalent to a 1% rise). This is discussed in more detail in section H in the report

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

Council Tax Increase

	0%	1%	4%
Band D Tax	67.36	68.03	68.7
District Precept	£m	£m	£m
LIVERPOOL	5.980	6.040	6.099
WIRRAL	5.868	5.927	5.985
ST.HELENS	3.115	3.146	3.177
SEFTON	5.154	5.205	5.257
KNOWSLEY	2.059	2.080	2.100
	22.176	22.398	22.618

Members must choose a portfolio of savings and growth options, a strategy for reserves (in the light of the advice of the Deputy Chief Executive) and a Council Tax level for 2013/14 that sets a balanced budget in line with the statutory timetable.

Capital

25. The proposed 5 year capital programme is detailed in section C. The table overleaf summarises the proposed investments which are mainly in the Authority's property, vehicle and ICT assets which total nearly £31.5million across the life of the programme. This capital programme is based on the

assumption that the Authority accepts the review of capital financing costs put forward by the Deputy Chief Executive.

Proposed Authority Capital Progamme for 2013/2014 - 2017/2018

Expenditure	Total Cost £	2013/14 £	2014/15 £	2015/16 £	2016/17 £	2017/18 £
Building/Land	**14,084,000**	10,144,000	1,031,000	1,976,500	560,500	372,000
Fire Safety	**6,403,000**	1,283,000	1,281,000	1,281,000	1,279,000	1,279,000
ICT	**3,138,000**	1,048,000	396,000	637,000	516,000	541,000
Operational Equipment & Hydrants	**1,485,000**	667,000	342,000	57,000	352,000	67,000
Vehicles	**6,374,100**	1,783,900	204,100	1,380,300	1,793,800	1,212,000
TOTAL	**31,484,100**	**14,925,900**	**3,254,100**	**5,331,800**	**4,501,300**	**3,471,000**

Financing Available:	Total	2013/14	2014/15	2015/16	2016/17	2017/18
Capital Receipts						
Toxteth Fire Station (Firefit Hub)	**250,000**	250,000				
Sale of 2 existing N-le-W LLAR properties	**275,000**			275,000		
Sale of LLAR house Cable Street, Formby	**350,000**	350,000				
Sale of Derby Road	**700,000**	700,000				
R.C.C.O.						
CFS alarm installation (salaries)	**3,650,000**	730,000	730,000	730,000	730,000	730,000
Capital Reserve to Gym Equipment	**50,000**	50,000				
Capital Reserve to JCC	**1,768,000**	1,768,000				
Grant						
Toxteth Hub: My Space Big Lottery Grant	**2,487,932**	1,243,966	1,243,966			
CLG Fire Control Grant (£1.8m in total)	**1,100,000**	1,100,000				
Other						
JCC Merseyside Police Contribution	**4,002,000**	4,002,000				
Total Non Borrowing	**14,632,932**	**10,193,966**	**1,973,966**	**1,005,000**	**730,000**	**730,000**
Unsupported Borrowing	**16,851,168**	4,731,934	1,280,134	4,326,800	3,771,300	2,741,000
Total Funding	**31,484,100**	**14,925,900**	**3,254,100**	**5,331,800**	**4,501,300**	**3,471,000**

26. This capital programme has a borrowing requirement of £4.732million in 2013/14 and £16.851million across the whole life of the plan. The proposed borrowing is unsupported borrowing or prudential as Members will note that the Government no longer allocates any supported borrowing to fire authorities and therefore no longer builds any revenue grant funding support for new borrowing in the formula grant. This means all borrowing is prudential.

27. The Government has announced the Authority will receive a general capital grant in 2013/14 and 2014/15 of £1.244m p.a. and this has been taken into account in determining the Authority's borrowing requirement over the life of the above capital programme. In addition the Authority has been awarded a specific capital grant of £1.770m for the new fire station proposal at Prescot, this scheme and associated grant have not been built into the capital programme at this stage as the project is still being finalised.

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

29. There has been an increase in Authority debt levels in recent years as the service needed significant capital infrastructure investment following a long period of restricted capital spend under previous capital control regimes. Current and future debt servicing costs as a consequence of the proposed capital programme have been built into the proposed financial plan. This report provides members with a number of prudential indicators so they can ensure that this commitment is considered affordable, prudent and sustainable in light of these prudential indicators (Section E).

Treasury Management

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

31. 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

32. 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.

33. The Deputy Chief Executive has reviewed the MRP policy in line with the legislation and the report outlines the proposed MRP policy for 2013/14 and future years.

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

B) BACKGROUND INFORMATION

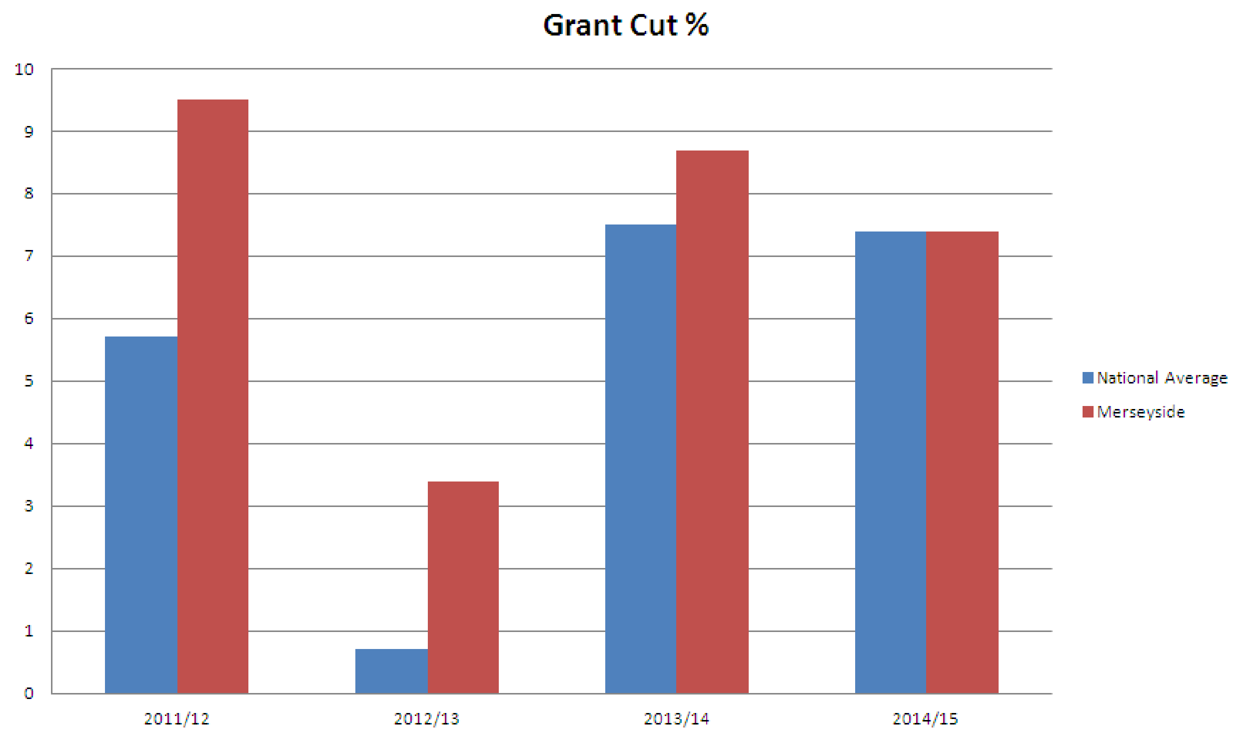
35. This section provides general financial information on the Authority's finances and financial health.

Corporate Strategy

36. If any organisation wants to be successful its budget setting and medium term financial plan must allocate resources to support its key strategic aims and priorities. This is a vital consideration when organisations face periods of severe resource shortages.

37. For many years now the Authority has maintained a comprehensive five year financial plan and capital programme despite facing significant financial challenges as a result of ongoing poor Government grant settlements for the Authority. In 2010 the new Government announced its spending review targets for 2011/12 – 2014/15 in which it stated that fire authorities faced a 25% reduction in government funding (equivalent to a cash reduction of 18%) over this period. The Government stated the reduction will be back loaded for fire authorities, with approximately 1/3rd of the reduction in the first two financial years, (2011/12 – 2012/13) and the remainder in the last two years.

The Government has announced the Authority's grant settlement figures for 2011/12, 2012/13 and 2013/14**,** with an indicative figure for 2014/15, **overall MFRA's grant has been cut by 26% compared to a national average grant cut of 19.9% over the four year period.** The table below outlines the grant changes for MFRA and the national average over this period:



38. In addition to the £9.2m saving identified already (2011/12 & 2012/13) the Authority must now identify additional savings to offset the budget challenge over the 2013/14 and 2014/15 period. It is likely further cuts in grant will be seen in 2015/16 and future years based on Government announcements.

39. 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.

40. The Authority's IRMP states the main strategic themes that the Authority has been progressing and its plans for the future. The 2013/14 IRMP, report CFO/024/13 is also considered as part of the budget meeting and appears elsewhere on the agenda. The IRMP is a three year plan and 2013/14 is the second year of the current plan.

41. The Authority's key Mission and Aims as set out in the IRMP are repeated out below. Any financial plan should aim to allocate resources to deliver that mission and aims.

Our Mission;

To Achieve; Safer Stronger Communities - Safe Effective Firefighters

Our Aims;

Excellent Operational Preparedness
We will provide our firefighters with the training, information, procedures and equipment to ensure they can safely and effectively resolve all emergency incidents.

Excellent Operational Response
To maintain an excellent emergency response to meet risk across Merseyside with safety and effectiveness at its core.

Excellent Prevention and Protection
We will work with our partners and our community to protect the most vulnerable through targeted local risk reduction, health inequality intervention and the robust application of our legal powers.

Excellent People
We will develop and value all our employees, respecting diversity, promoting opportunity and equality for all.

Is the Overall Strategy Working?

42. The Fire Authority has achieved great success in its aims to make Merseyside a safer community over the last decade. Members receive detail on this excellent performance in a variety of formats but highlights include:-

(a) Becoming the first fire authority in the world to visit 100,000 households in a single year to carry out Home Fire safety Checks (and approximately 700,000 visits in total have been carried out).

(b) Fitting approximately 800,000 smoke alarms.

(c) Significantly reducing the impact of antisocial behaviour during the bonfire period through effective joint working with partners. During the 2012 bonfire period Merseyside Fire and Rescue Service attended 427 anti-social behaviour fires against 1,250 during 2004, a reduction of 66%

(d) Reducing fire deaths from an average of 20 in 1999 to 5 in 2010/11 and to 2 confirmed and potentially another 2 so far this year (year ends March), a +75% reduction.

(e) Reduced the total number of all types of fires and their impacts.

43. The table below summarises some key performance statistics over the last 9 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	1299	117	8	7384
2010-2011	1199	137	5	6893
2011 – 2012	1195	131	5	6042
2012 - 13 Q3	812	84	2	3090
Reduction between 2003/04 to 2011/12	-49.63%	-50.88%	-77.78%	-83.72%

Financial Strategy and where are we now?

44. 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 and trained employees 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
- Invested to maintain emergency response standards and to modernise working arrangements for dealing with a whole host of emergency incidents

- Developed arrangements for restoration with the private sector and the Fire Support Network

- Made significant investment in IT and computing (including outsourcing)

- Provided further investment in equality and health and safety

- Attempted to plan prudently over the medium term by considering all significant risks to the assumptions in the financial plan and creating specific reserves if deemed necessary

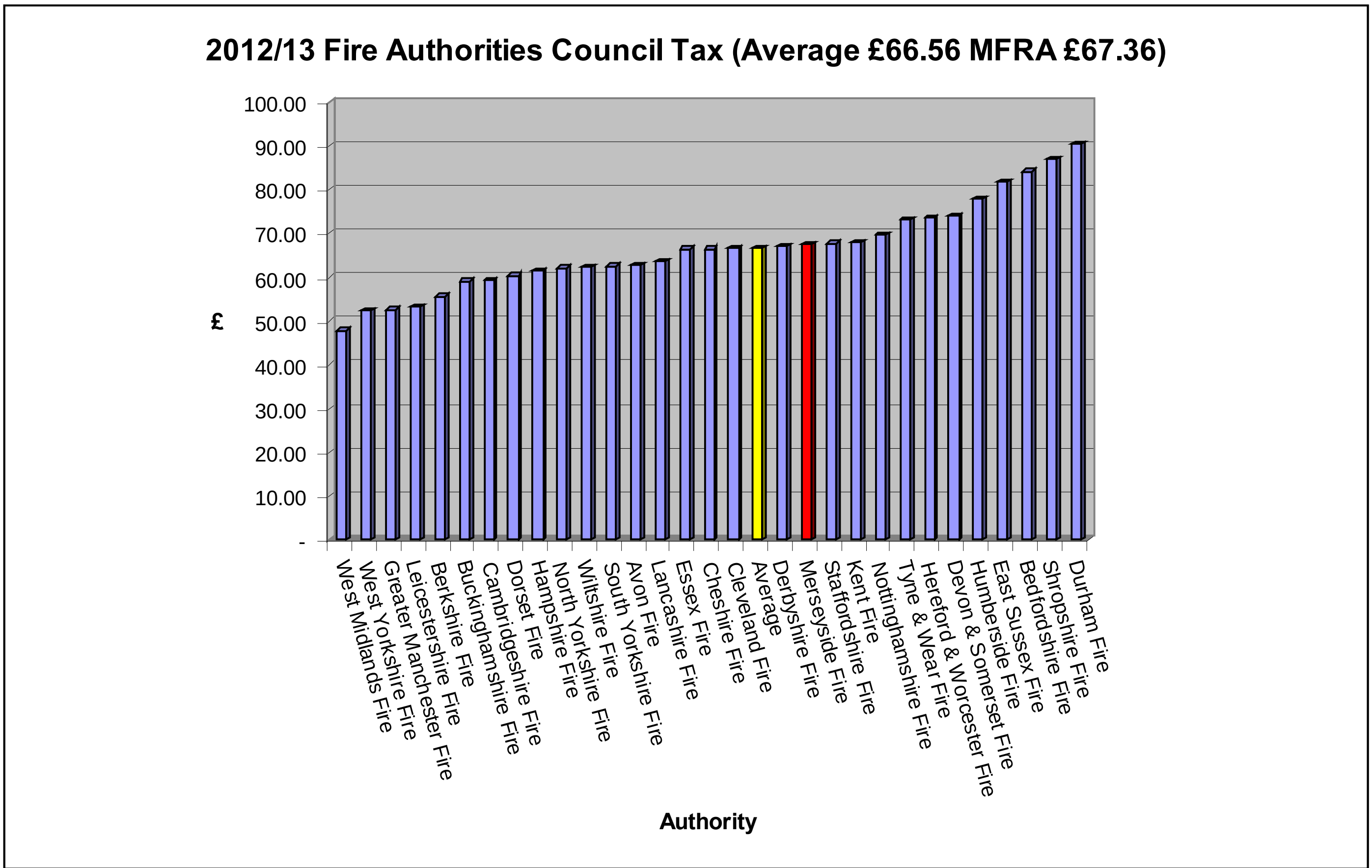
- Maintained a general fund reserve of at least £2m following assessments of risk

- Because of pressures on revenue budget generally avoided funding capital expenditure from revenue through leasing or RCCO

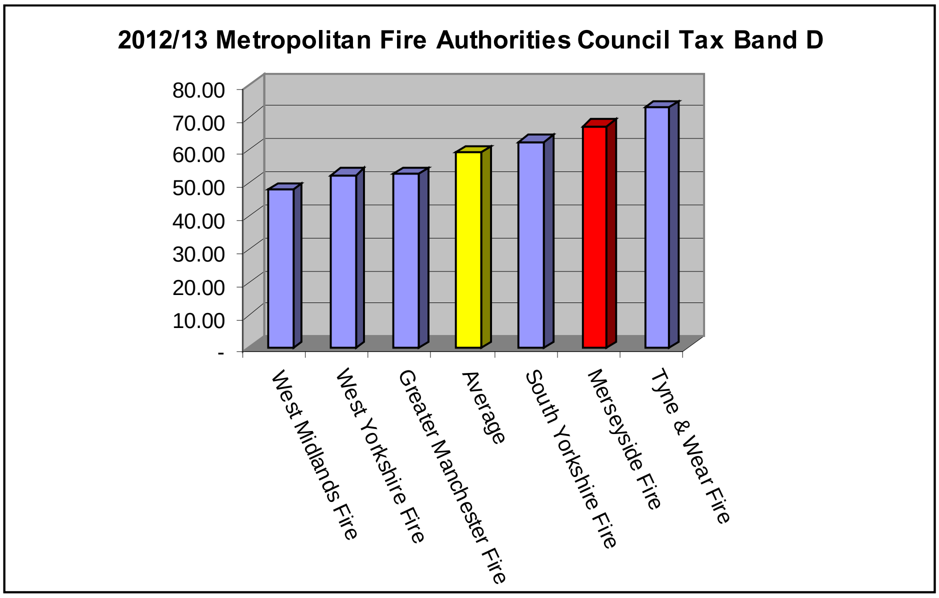
- Invested in the capital infrastructure of the Authority in line with the Asset Management Plan, vehicle replacement strategies and corporate objectives.

These strategies have over recent history allowed the Authority to make significant strides in reducing cost and maintaining relatively low levels of Council Tax increase despite very tight grant settlements.

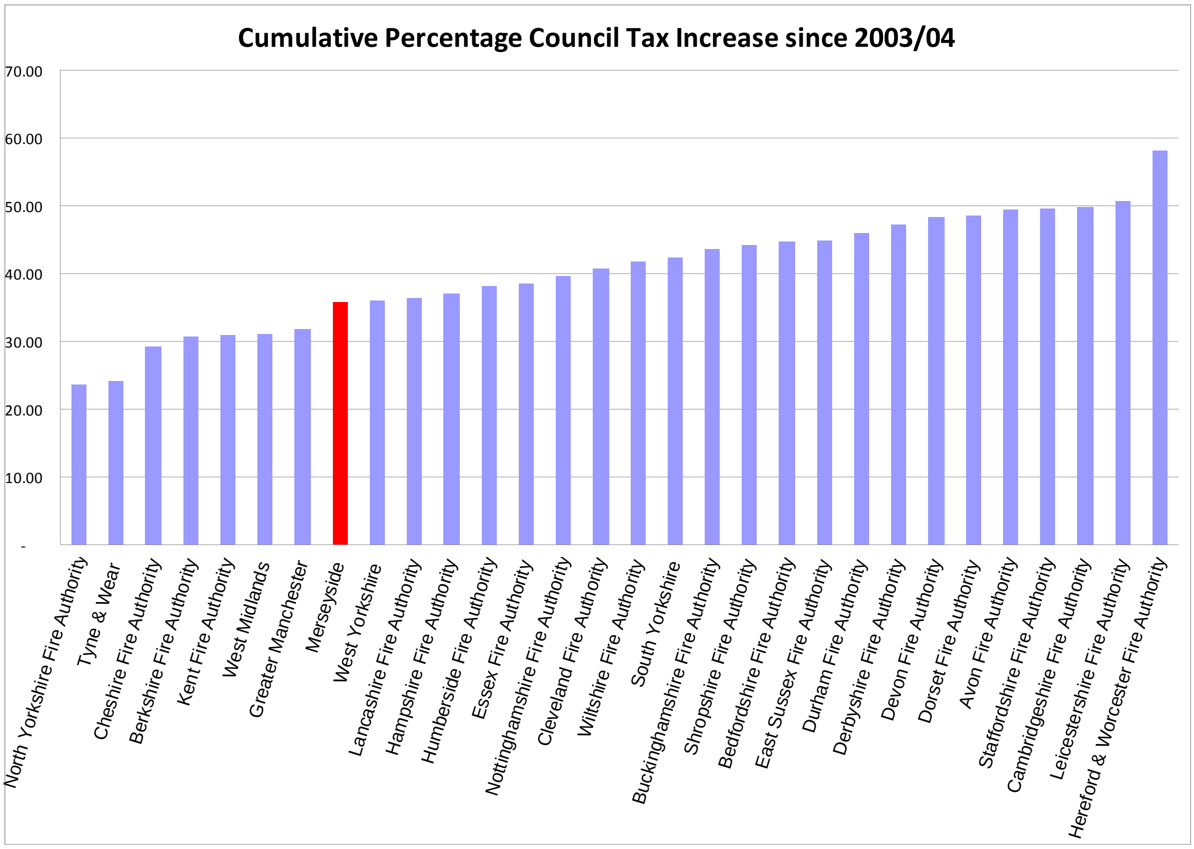
The Authority is slightly above the national average Band D council tax for fire services;



In 1996/97 Merseyside's Council Tax was more than 50% above the average of Metropolitan Fire Authorities. Now it is only 13.5% above the average:

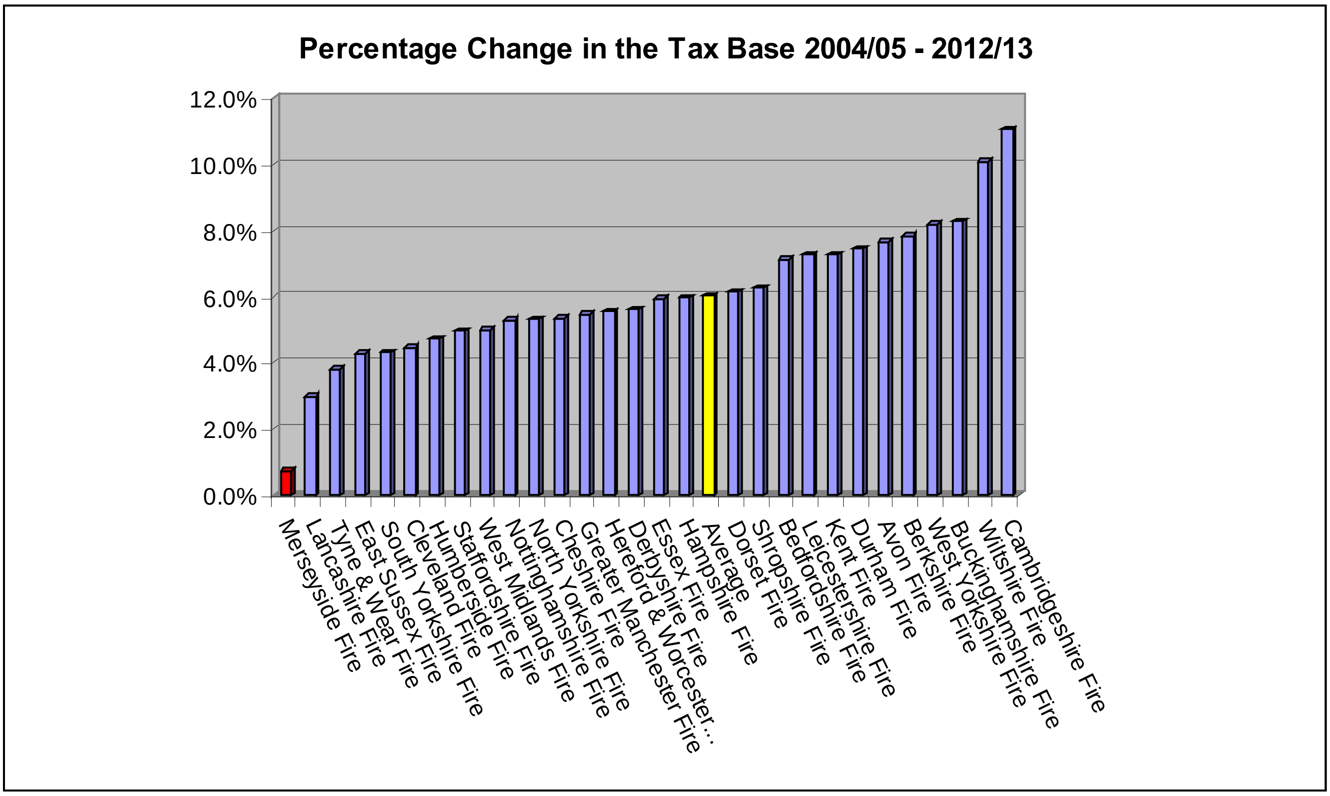


Over the past 9 years when compared to the other Fire Authorities Merseyside has had one of the lowest cumulative council tax increases:

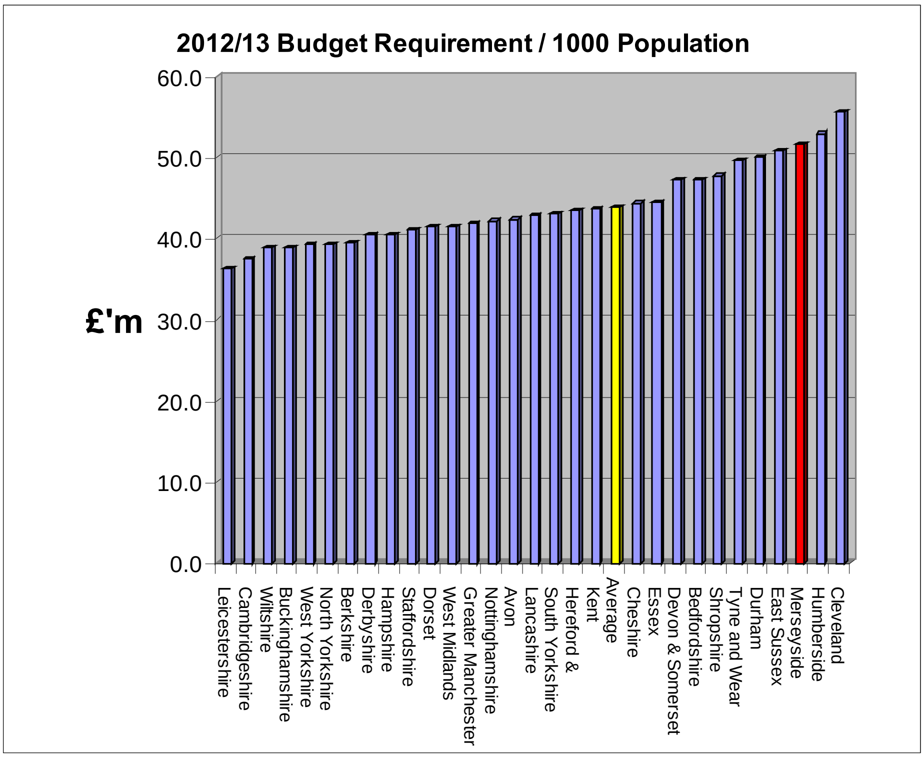


The significant improvements in efficiency by the Fire Authority and a large scale savings plan have meant that from being one of the most expensive fire authorities in the country in 2000/01 the Authority has now, at £67.36 per Band D household, moved closer to the fire average (£66.56).

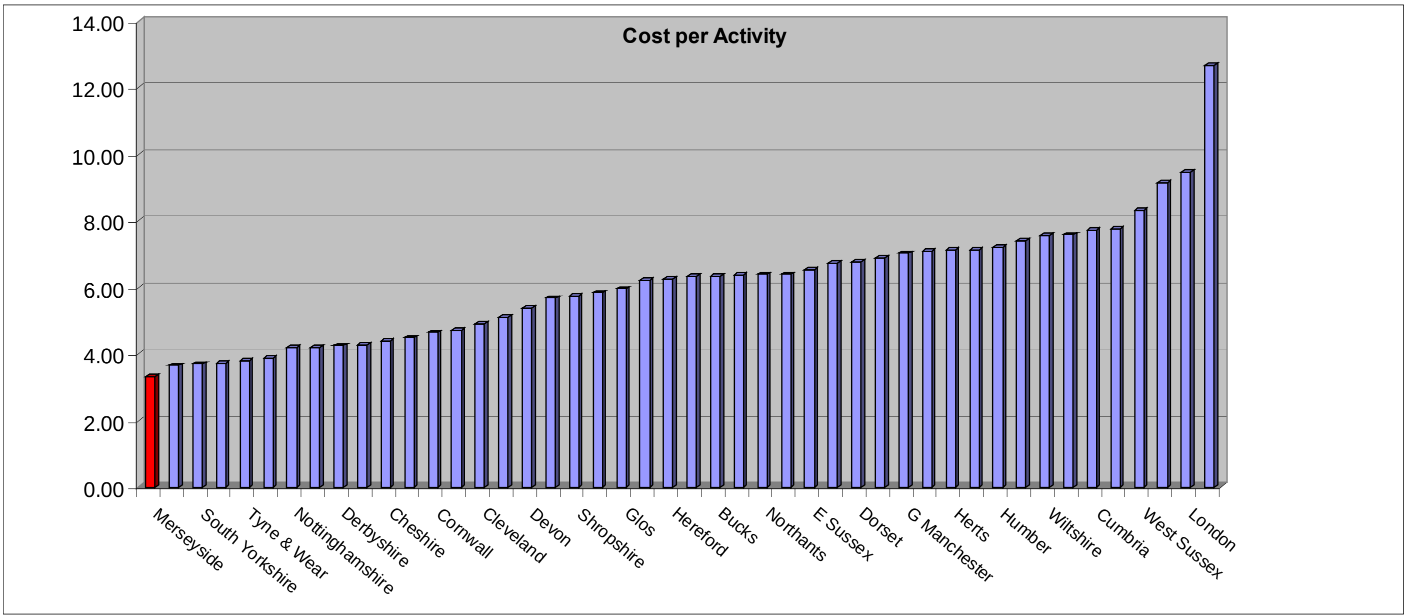
This performance has been especially encouraging when it is considered that across the same time period the council tax base of Merseyside has increased by +0.7% against a national average of +6%, and the highest authority increase of 11%. *If all other things had been equal it might have been expected 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.

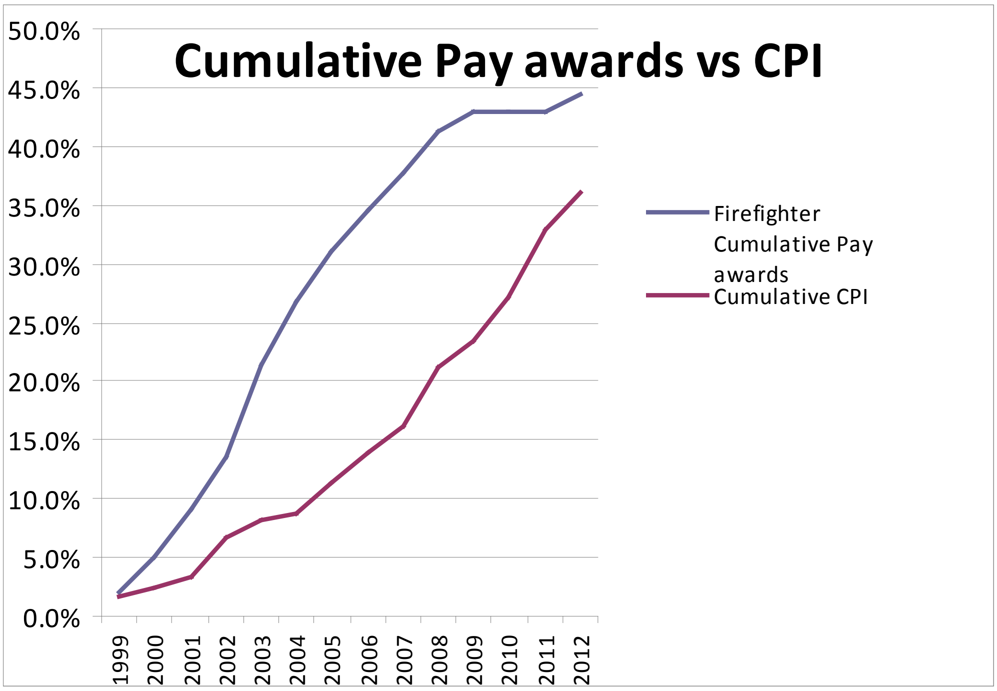


It should be noted that this is only one measure of the relative need to spend (population basis). A comparison of **historic** net expenditure per activity (including home fire safety checks) over recent years shows a very different picture:



Merseyside continues to invest significantly in community fire safety, approximately £6million in 2012/13.

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 has on average been very much higher. The table below highlights cumulative Firefighter pay increases compared to consumer price index since 2000.



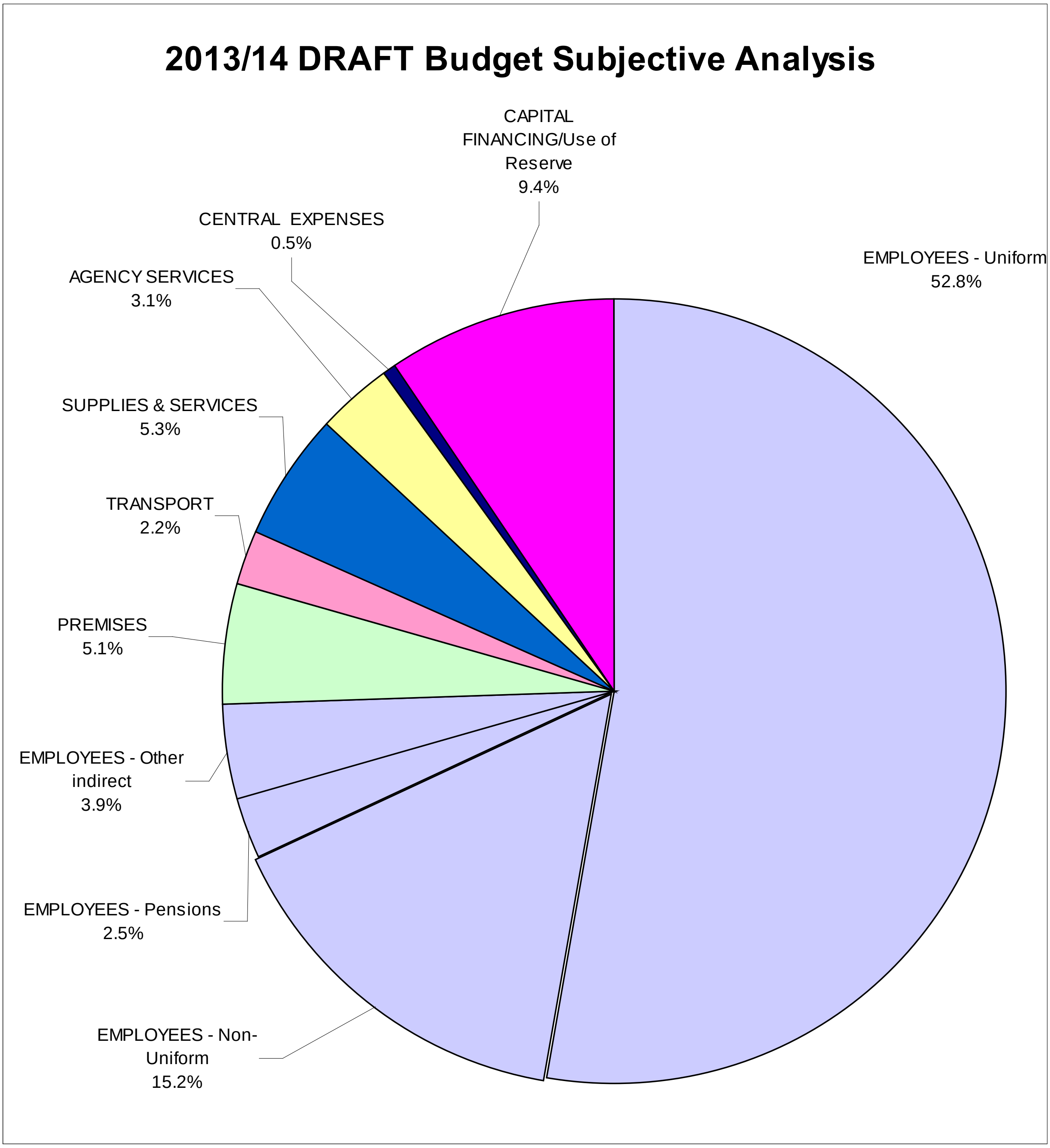
Overall Financial Health

45. The Authority has a proven track record for meeting significant financial challenges in the past and modernising the service to maintain if not improve the service to the community of Merseyside. The Authority, conscious of the pending financial challenge, has built up reserves in recent years as part of a strategy to provide a short term buffer whilst the Authority implements the business re-engineering to deliver the required savings on a permanent basis. The unprecedented reductions in Government funding will require innovative and difficult decisions but the Authority has a proven track record in managing its financial affairs well as can be seen in the following indicators:-

- Authority accounts 2011/12 audited without qualification once 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 (now £4.7m) in recent years.
- Cost centre budgeting now well established along with a culture of financial management.
- Maintained a five year financial plan and capital programme and most importantly a consistent medium term strategy.
- Successfully delivered large-scale changes and savings

Current Allocation of Resources

46. Members will be aware that Fire Service expenditure is predominantly employee related costs (approximately 75%) as is shown in the pie chart below. (The lilac sections relate to employee costs)

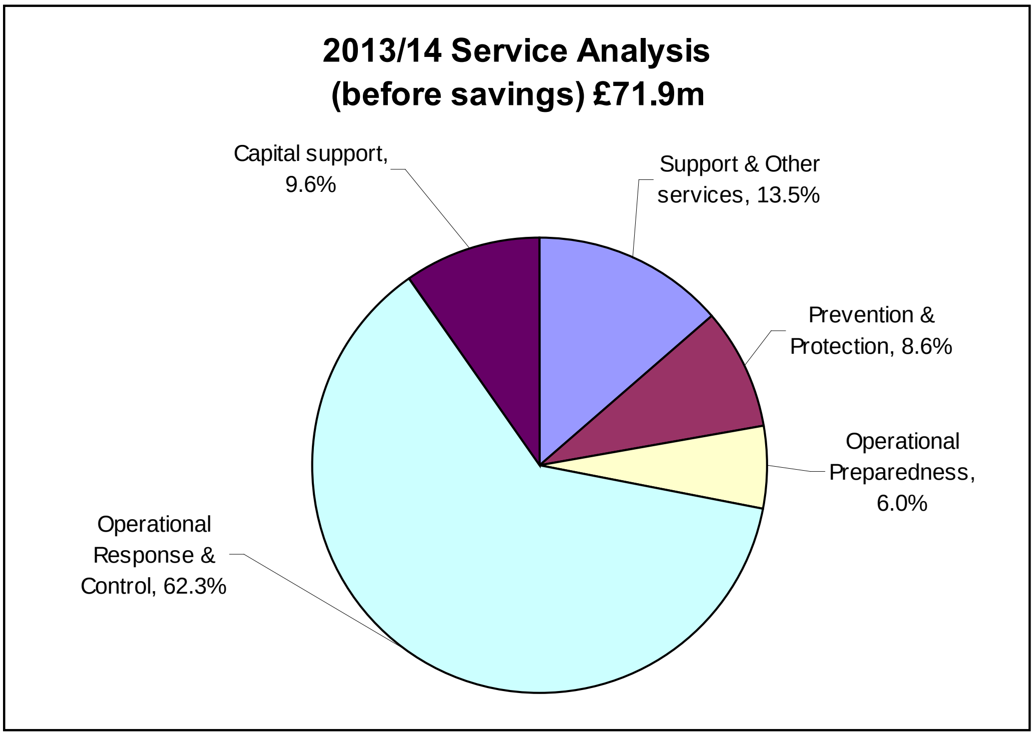


A full subjective analysis of the base budget for 2013/14 is set out in **Appendix 1**

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 overleaf and is based upon the service's strategic objectives:

Allocation of Resources in line with Corporate Objectives

47. The Authority has an excellent track record of investing in line with its corporate priorities. It can be seen from the pie chart below that 62.3% of expenditure goes on emergency and specialist response; 6.0% on Operational Preparedness; 8.6% on Prevention & Protection, and therefore over 76.9% of expenditure is on the “front line” services. In addition the 9.6% on servicing previous capital investment relates mostly to front line assets, fire stations, vehicles and equipment. The remaining 13.5% is on support services.



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

Operational Response & Control

Investing £45m

- Service delivery and emergency response through its 26 fire stations.
- Specialist teams like Search and Rescue Team, Targeted Response Group, Hazmats Team and Emergency Response Dogs .
- Invested in staff safety – procured effective fire kit, helmets, boots and appliances.
- Invests £0.5m on the Incident Management Team.
- Deliver HFSC programme.
- Investing in new community fire stations.

Prevention & Protection

Investing £6m p.a in prevention & protection including:

- Protection Teams; £1.5m
- Purchase of £0.5m worth of smoke alarms per annum
- Fire Service Direct; £0.2m
- Employment of specialist Advocates continuation of the Princes Trust and other programmes; £0.2m

- Other specialist teams; Fireworks; Arson; Crime Prevention; £0.2m
- Working with young people, including school liaison
- Invested in volunteers with the Fire Support Network; £0.2m
- District prevention teams; £1.7m
- Working with the private sector to deliver speedier restoration of property

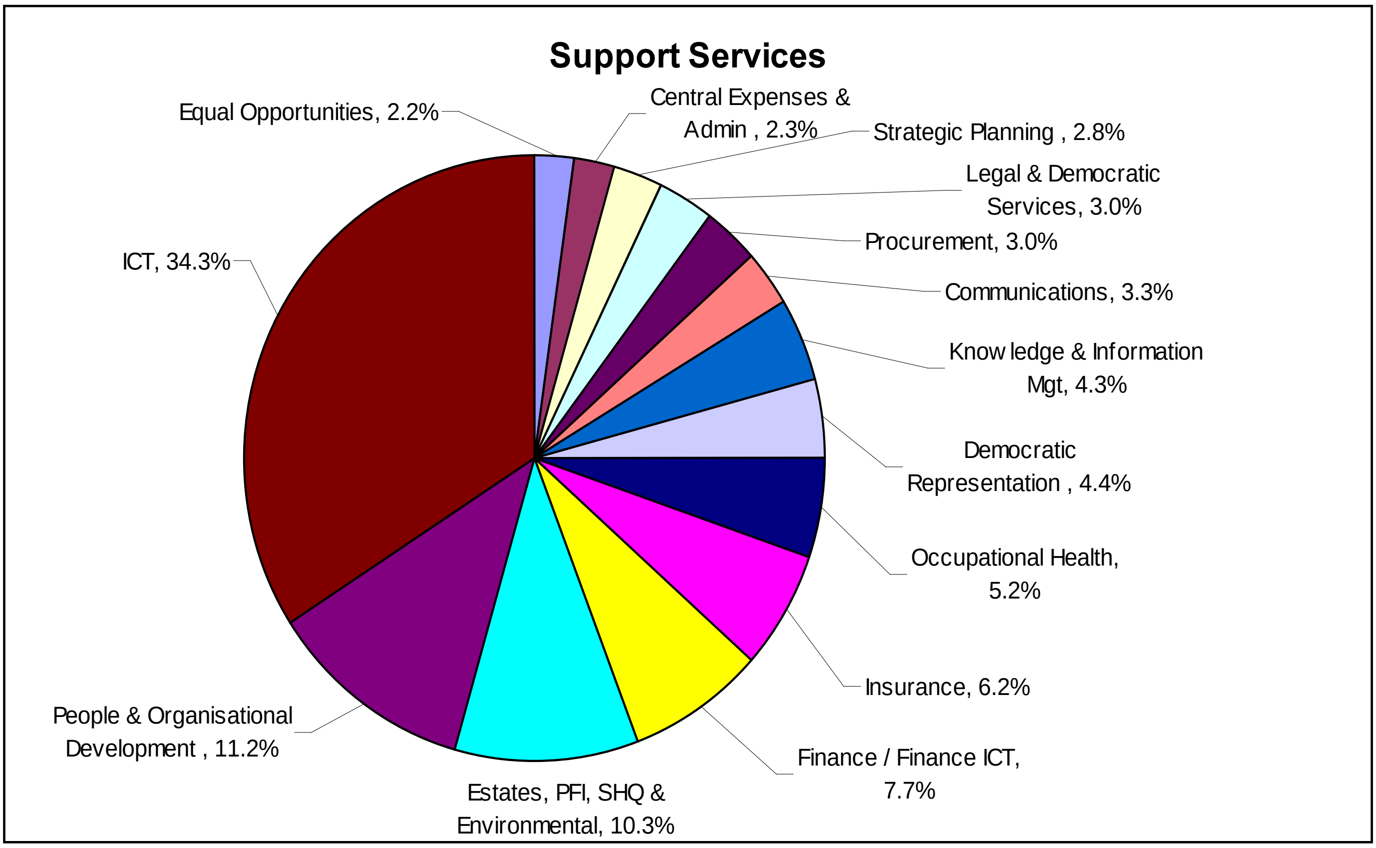
Operational Preparedness

The investment of over £4m delivers a variety of services which helps prepare for a full range of possible incidents in Merseyside 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

The investment in support services of £10m (14% of the budget) is analysed below:



It should be noted that many of the services are key “front line” parts of a modern fire and rescue service. For example:-

- People and Organisation Development – includes investment in the Training and Development Academy and costs of training for all staff;
- Estates – includes the running costs of buildings including 26 Community Fire Stations;
- ICT – includes the cost of the Mobilising Communications Centre;

C) CAPITAL PROGRAMME

48. 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. ***The following sections C) to F) anticipate the Authority agreeing to the outcomes of the capital programme and financing review undertaken by the Deputy Chief Executive.***

Introduction

49. From 1st April 2004, the Local Government Act 2003 replaced the previous regime of capital controls with the Prudential System for Capital Finance. Local authorities are free 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

50. A key part of the revised 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.

51. 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.

52. 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.

53. 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.

54. 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.

Capital Investment Strategy .

55. 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.

56. The starting point for this programme has been an assessment of the capital investment 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.

57. This has produced a total 2013/14 – 2017/18 five-year future capital programme proposal of £31.484m which is set out in the summary table overleaf. This table also identifies funding of the programme and a borrowing requirement of £16.851m to support the proposed capital programme. The full programme is set out in **Appendix 2** (Appendix 2 (A) is the updated programme and appendix 2(B) the new additions to previously agreed programmes).

Proposed Authority Capital Progamme for 2013/2014 - 2017/2018

Expenditure	Total Cost £	2013/14 £	2014/15 £	2015/16 £	2016/17 £	2017/18 £
Building/Land	**14,084,000**	10,144,000	1,031,000	1,976,500	560,500	372,000
Fire Safety	**6,403,000**	1,283,000	1,281,000	1,281,000	1,279,000	1,279,000
ICT	**3,138,000**	1,048,000	396,000	637,000	516,000	541,000
Operational Equipment & Hydrants	**1,485,000**	667,000	342,000	57,000	352,000	67,000
Vehicles	**6,374,100**	1,783,900	204,100	1,380,300	1,793,800	1,212,000
TOTAL	**31,484,100**	**14,925,900**	**3,254,100**	**5,331,800**	**4,501,300**	**3,471,000**

Financing Available:	Total	2013/14	2014/15	2015/16	2016/17	2017/18
Capital Receipts						
Toxteth Fire Station (Firefit Hub)	**250,000**	250,000				
Sale of 2 existing N-le-W LLAR properties	**275,000**			275,000		
Sale of LLAR house Cable Street, Formby	**350,000**	350,000				
Sale of Derby Road	**700,000**	700,000				
R.C.C.O.						
CFS alarm installation (salaries)	**3,650,000**	730,000	730,000	730,000	730,000	730,000
Capital Reserve to Gym Equipment	**50,000**	50,000				
Capital Reserve to JCC	**1,768,000**	1,768,000				
Grant						
Toxteth Hub: My Space Big Lottery Grant	**2,487,932**	1,243,966	1,243,966			
CLG Fire Control Grant (£1.8m in total)	**1,100,000**	1,100,000				
Other						
JCC Merseyside Police Contribution	**4,002,000**	4,002,000				
Total Non Borrowing	**14,632,932**	**10,193,966**	**1,973,966**	**1,005,000**	**730,000**	**730,000**
Unsupported Borrowing	**16,851,168**	4,731,934	1,280,134	4,326,800	3,771,300	2,741,000
Total Funding	**31,484,100**	**14,925,900**	**3,254,100**	**5,331,800**	**4,501,300**	**3,471,000**

58. The revised capital programme has increased the overall expenditure by £0.386m, (Appendix 2b), the reasons for this are summarised below:-

    (a) The addition of the “extra year” to the programme 2017/18, £3.471m
    (b) Amendments to the 2013/14 – 2016/17 programme, which in total reduced it by -£3.085m, that reflect a reduction in the anticipated vehicle fleet and the free smoke alarm programme.

59. 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 the current financial review (CFO/024/13), elsewhere on the agenda, details the movements on the approved capital plan during the financial year .

60. The key areas of investment (2013/14 -2017/18) are:-

<u>Building Investment Strategy (£14.084m)</u>

61. The estate comprises of 26 fire stations, a Training and Development Academy (TDA), a Mobilising & Communication Centre (MACC), Service Headquarters, Marine 1, and the Engineering Centre. 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 maintain and revise a 5 year property asset management plan and the proposed capital programme is consistent with the priority areas that are contained within the plan.

    <u>PFI</u>

62. The Government has approved a joint project (with Merseyside leading), between Merseyside, Lancashire and Cumbria. In Merseyside there will be seven new stations at:-

    a. Belle Vale
    b. Birkenhead
    c. Bootle/Netherton
    d. Formby
    e. Kirkdale (with Operational Resource Centre (ORC) on same site)
    f. Newton le Willows
    g. Southport (combined Fire and Ambulance Station)

63. Building work for the stations at Bootle/Netherton, Formby, Kirkdale and Newton le Willows is complete and all stations are now in use. The Ambulance Service is sharing the stations at Formby and Newton le Willows. Work on the stations at Belle Vale, Birkenhead and Southport is progressing well and these should be ready for occupation in mid 2013.

64. The total capital building costs for the North West building stock will be £47.9m (October 2010 prices) and in Merseyside £19.8m. As the capital expenditure will not go through the Authority’s capital programme this scheme is not

included in the current capital programme. Changes to the accounting rules mean that 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).

Non PFI Project Assets

65. For those properties which don't form part of the PFI project investment is proposed in line with the current Asset Management Plan. Notable projects include:-

a. The construction of a new Joint Control room at SHQ with Merseyside Police, £7.6m
b. Refurbishing and essential work at fire stations £4.8m
c. LLAR accommodation £0.6m

Fire Safety (£6.403m)

66. Smoke alarms and sprinkler systems are being classed as capital expenditure in line with Government guidance. This follows the awarding of historic capital grants by the (then) ODPM towards the purchase cost of such items in financial years 2004/05 through to 2007/08. The estimated investment in alarms for the community over the 2013/14 – 2017/18 period has been reduced, in anticipation of the Authority approving significant savings in front line HFSC delivery, to £0.5m p.a, slightly less than in previous years but it is sufficient to continue the provision of free alarms for high risk vulnerable groups. Current policy is to capitalise the installation costs of smoke alarms estimated at £3.65m over the period, however this expenditure is not funded through borrowing but financed in the year by a revenue contribution to capital.

ICT – Investing in line with the ICT Strategy (£3.138m)

67. 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 £1.8m, and software licenses £0.4m.

68. Specific projects include:-

a. Continued development of the portal, £0.2m,
b. Computerisation of the HR & training records, £0.2m
c. Planned replacement of the current Finance, payroll and procurement ICT systems, £0.2m

Operational Equipment & Hydrants (£1.485m)

69. Significant provision is also made to ensure that a modern fire and rescue service can be delivered and firefighters kept safe, in particular provision is made for investment in specialist rescue equipment and new breathing apparatus such as :-

- Hydraulic Rescue equipment, £0.2m
- Specialist emergency & rescue equipment, £0.8m
- Installation of new or replacement hydrants in line with our water strategy, £0.2m.

Vehicle Replacement Strategy (£6.374m)

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

WTL Fire Appliances

71. The Authority has developed an appliance replacement strategy based on the economic life of an appliance. Each appliance has an estimated service life of 12 years on the front line followed by 2 years as a reserve appliance. In addition in light of the impact of the on-going financial challenge and expected number of appliances to be held in a dynamic reserve officers have identified that the service does not need to procure any new appliances in 2013/14 and 2014/15. The plan does provide for 12 new appliances (2015/16-2017/18) to ensure that the fleet is modern and efficient. .

A Need for Specialist Vehicles

72. 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:

a. Combined Pump Platform appliances (2 refurbished and 1 new vehicle)
b. IMU - Prime Movers (6)
c. Special Vehicles (Water Rescue, BA Support unit)

Ancillary Vehicles

73. Provision is included for the phased renewal of the ancillary vehicle fleet. These are increasingly important to support the fire safety and prevention work of the Service.

74. The CFO is reviewing the profile of the investment in specialist and ancillary vehicles in light of service cuts and need.

Funding The Programme

Capital Receipts

75. 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.

76. 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 if a proportion of any future receipts should be used for debt repayment as part of its overall strategy.

77. The proposed capital programme anticipates capital receipts from the following site sales: -

Toxteth Fire Station	£0.250m	(2013/14)
Derby Road	£0.700m	(2013/14)
LLAR House Formby	£0.350m	(2013/14)
Existing LLAR Houses Newton-le-Willows	£0.275m	(2015/16)

78. It assumes that this income will be used to reinvest in the capital infrastructure and support the capital programme. Members should note that the valuations are based on recent valuations.

<u>Capital Grants</u>

79. As part of the 2010 spending review the Government also made the decision that there will be no supported borrowing allocations for the fire and rescue service in the spending review period. Government capital support will be given in the form of capital grant only. The Government has announced that the Authority will receive a £1.244m general capital grant in 2013/14 and 2014/15 and these grants have been taken into account in the current capital programme. In addition the Authority will receive a specific capital grant of £1.770m for a new joint blue light station at Prescot in line with its bid, this scheme and associated grant have not been built into the capital programme at this stage as the project is still being finalised.

<u>Alternative to Operating Leasing</u>

80. Under the previous system of capital controls, investment that was funded by operating leases 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, plant 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 Deputy Chief Executive will monitor the suitability of alternative methods of finance.

<u>Borrowing</u>

81. Under the Prudential capital system Local Authorities are now able to determine their level of borrowing. 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.

82. In the past Government provided support for the Authority's capital spending through **supported** capital expenditure. The revenue costs associated with supported borrowing was funded through the revenue formula grant. As part of the CSR2010, the Government made the decision that no new supported borrowing allocations will be made to the Fire and Rescue Service in the Spending Review period. This will impact on revenue support grant allocations. Whilst there will be no new allocations after 2010/11, the level of assumed outstanding historic debt still forms part of the Formula Grant calculation and hence the Authority still receives some grant funding. **All** borrowing from 2011/12 is therefore effectively now unsupported or prudential borrowing.

83. The proposed capital programme represents an overall expenditure increase of £0.386m reflecting the proposed "new starts" expenditure, of which £3.471m relates to the addition of 2017/18, and the net reduction in planned expenditure in 2013/14 – 2016/17 of £3.085m. Appendix 2B sets out these changes in more detail.

84. The impact of these net additions to the programme on the Authority's borrowing is a net increase of £0.736:

	£m
Increase in net expenditure	0.4
Change in Non Borrowing Funding Sources:	
• RCCO (HFSC installation costs)	0.3
Required Increase in Borrowing	0.7

The level of prudential "unsupported" borrowing therefore will increase by £0.736m to £16.851m.

Impacts on Revenue Budget and Financial Plan

85. 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 2013/14 – 2017/18 and the methodology for calculating the MRP. The additional borrowing and proposed MRP policy require an increase to the 2012/13 base figure for MRP and Interest of:-

	Estimate 20013/14	Estimate 20014/15	Estimate 2015/16	Estimate 2016/17	Estimate 2017/18
	£'m	£'m	£'m	£'m	£'m
Cummulative Increase in MRP / Interest	**0.362**	**0.877**	**0.974**	**1.416**	**1.705**

86. A significant factor in the large increase in the budget requirement is down to the Government's decision to factor in no new supported borrowing in the 2011/12 or future years grant settlement and the capital regulations requiring all non-supported borrowing to be repaid over the relevant asset life. This has meant a four or five fold increase in MRP calculations for assets with a short asset life that previously had MRP calculated over a twenty-five year period.

87. Anticipated increase in MRP and Interest had already been built into the proposed financial plan for 2013/14 – 2017/18. To give Members an indication of the impact of the proposals, for each £1M reduction in borrowing it would reduce the associated revenue cost by potentially £0.050m - £0.100m (depends on the relevant asset life), the council tax equivalent reduction would be 0.2% - 0.5% or £0.13 to £0.34.

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

(D) MINIMUM REVENUE PROVISION STATEMENT

88. 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.

89. 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).

90. The regulations guidelines set out four options for calculating MRP; (however as the Government are issuing no new supported borrowing only 2 of the 4 options are applicable for new borrowing; Asset Life or Depreciation methods):

- **Regulatory Method** – This provides for local authorities to continue to calculate MRP in line with the minimum existing statutory charge of 4% of outstanding debt related to supported borrowing only. This option is available for all capital expenditure incurred prior to 1 April 2008.

- **Capital Financing Requirement Method** – This is very similar to the regulatory method but it does not take account of the adjustment that ensures authorities do not pay more MRP than under the previous capital regulatory regimes. For most authorities this method may not be appropriate as it would result in a higher level of provision than option 1.

- **Asset Life Method** – MRP is determined by reference to the life of the asset and the amount is either based on;

    - o **equal instalments method.** This generates a series of equal annual amounts over the life of each asset that is financed from borrowing; or

    - o **annuity method.** This method links the MRP to the flow of benefits from an asset where the benefit is expected to increase in later years.

  These options are available to both supported and unsupported borrowing in determining the MRP requirement.

Finance Leases and PFI
The guidance indicates that for finance leases and on balance sheet PFI contracts, the MRP requirement is met by making a charge equal to the element of the finance lease rental that goes to write down the balance sheet liability under proper accounting practices. This is in effect a modified version of the asset life - annuity method, the impact on the revenue account is neutral with MRP for these items matching the principal repayment embedded within the PFI or lease agreement.

- **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

2013/14 MRP:

91. The 2013/14 MRP is determined by the actual level of outstanding debt (CFR) as at the end of 2012/13. It is recommend that the Authority adopt a similar strategy for MRP determination as that in 2012/13;

- For all capital expenditure incurred before 1 April 2008 and for all capital expenditure funded via **supported borrowing**; MRP to be calculated using the Regulatory Method.

- For all capital expenditure incurred after 1 April 2008 financed by **unsupported (prudential) borrowing**; MRP to be calculated using the Asset Life Method – equal instalments method.

- For credit arrangements such as **on balance sheet leasing arrangements (finance leases)**; the MRP charge is to be equal to the principal element of the annual rental.

- For **on balance sheet PFI contracts**; the MRP charge will be equal to the principal element of the annual rental

92. The above options meet the requirement for MRP to be deemed prudent but also allows certainty and predictability over MRP charges. The financial plan outlined in this report reflects the proposed Authority's policy on prudential MRP.

93. By adopting the recommendations above the MRP charge for 2013/14 would be £3.280m, consisting of £1.289m for prudential borrowing schemes incurred after 1st April 2008, £1.991m for all other capital schemes and £0.022m for PFI & finance lease assets. This amount has been included within the budget estimate for 2013/14.

94. In addition it is proposed that if any approved MRP/Interest budget becomes available due to; capital schemes being re-phased; additional specific non-borrowing funding becoming available; or a reduction on the approved capital programme/ required borrowing, then the Service may choose to make additional MRP payments if the overall financial position of the Authority in that year remains consistent with the approved financial plan.

95. The Authority in the past has determined it can afford and sustain significant prudential 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.

(E) PRUDENTIAL INDICATOR REPORT

96. Having formulated a draft Capital Programme, the Authority, in making final decisions upon that Capital Programme and Revenue Budget 2013/14, 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.

97. 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 2013/14.

98. The financial plans prepared in respect of the financial years 2014/15 and 2015/16 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 2% in 2013/14 and 2014/15 and then 4% thereafter has been made.

Prudential Indicators

99. 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.***

100. 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.

101. The prudential indicators for Merseyside are:-

a) Capital Expenditure

The actual capital expenditure that was incurred in 2011/12 and the estimates of capital expenditure to be incurred for the current and future years that are recommended for approval are:

	Actual 2011/12	Estimate 2012/13	Estimate 2013/14	Estimate 2014/15	Estimate 2015/16	Estimate 2016/17	Estimate 2017/18
	£000,s	£000,s	£000,s	£000,s	£000,s	£000,s	£000,s
Capital Expenditure	**5,714**	**11,524**	**14,926**	**3,254**	**5,331**	**4,502**	**3,471**

Members will note that the increase in expenditure in 2011/12 to 2012/13 reflects the year-end re-phasing of £4m of planned expenditure into 2012/13 at the end of 2011/12. In 2013/14 the inclusion of the major building project for the new Joint Control Room, £7.6m, explains why the total spend in this year appears significantly greater than that in other years. 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 2011/12 are:

	Actual 2011/12	Estimate 2012/13	Estimate 2013/14	Estimate 2014/15	Estimate 2015/16	Estimate 2016/17	Estimate 2017/18
Ratio of Financing costs to Net Revenue Stream	**7.17%**	**7.77%**	**8.64%**	**9.76%**	**10.00%**	**10.66%**	**10.84%**

This shows that forecast debt financing costs will increase from 8.64% in 2013/14 (based on the actual forecast capital spend in 2012/13) to 10.84% by 2017/18. As stated previously the impact of the Government's decision to issue no new supported borrowing for CSR10 has meant all MRP calculations are now based on asset life. This has resulted in a significant rise in MRP over the medium term, but eventually the ratio will fall as historic debt is repaid and all other debt is paid off over the life of the asset. This is also affected by the fact that whilst the Authority's debt is increasing its overall budget is reducing.

(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 2011/12	Estimate 2012/13	Estimate 2013/14	Estimate 2014/15	Estimate 2015/16	Estimate 2016/17	Estimate 2017/18
Incremental Impact of Capital Investment Decisions	-£1.35	£0.25	£2.77	-£0.34	-£0.07	-£0.07	£0.95

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. It is intended to show the marginal impact of the overall capital programme, and the decisions being made by the Authority, on the Council Tax levels. The re-phasing of expenditure from 2011/12 into 2012/13, and the relatively lower capital spend in 2014/15 to 2016/17 compared to 2011/12 have resulted in a negative or reduced incremental increases over that period. The new start programme in 2017/18 has resulted in the increase in 2017/18.

Capital Financing Requirement

102. In accordance with best 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.

103. 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 2012 are:

	Actual 31.3.12	Estimate 31.3.13	Estimate 31.3.14	Estimate 31.3.15	Estimate 31.3.16	Estimate 31.3.17	Estimate 31.3.18
	£000,s	**£000,s**	**£000,s**	**£000,s**	**£000,s**	**£000,s**	**£000,s**
Capital Financing Requirement	**55,915**	**58,009**	**59,397**	**56,896**	**57,356**	**56,870**	**55,090**

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

105. The Authority's CFR is expected to reach £55.090m by the end of 2017/18 compared to current levels (end of 2011/12) of £55.915m. This is less than that that anticipated in last year's capital programme, £61.531m, as the impact of the £3.2m general government capital grant over the 2012/13 – 2014/15 period and the reduction in smoke alarm and fire appliance spend reduces the level of borrowing requirement.

Net Borrowing and the Capital Financing Requirement

106. 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."

107. The Authority had no difficulty meeting this requirement in 2011/12, nor is any difficulty 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 2013/14

INTRODUCTION

108. This report sets out the expected treasury operations for this period, linked to the Authority's Budget, Medium Term Financial Plan, and Capital Programme. It is inextricably linked to delivering the Authority's mission and aims. It contains four key legislative requirements:-

(a) The Treasury Management Strategy Statement which sets out how the Authority's treasury service supports capital decisions, day to day treasury management and the limitations on activity through treasury prudential indicators. The key indicator is the Authorised Limit required by S3 of the Local Government Act 2003 and is in accordance with the CIPFA (The Chartered Institute of Public Finance & Accountancy) Codes of Practice.

(b) The reporting of the prudential indicators for external debt and the treasury management prudential indicators as required by the CIPFA Treasury Management Code of Practice.

(c) The investment strategy which sets out the Authority's criteria for choosing investment counterparties and limiting exposure to the risk of loss. This strategy is in accordance with the Department for Communities and Local Government (DCLG) Guidance on Local Government Investments updated in 2010. It is proposed to maintain the Authority's minimum long term credit rating requirement of Fitch A- or equivalent.

(d) The Authority's Minimum Revenue Provision (MRP) Policy, which sets out how the Authority will pay for capital assets through revenue each year as required by Local Authorities (Capital Finance and Accounting) Regulations 2008.

RECOMMENDATIONS; PROPOSED STRATEGY

109. 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 recommended to approve each of the key elements contained within this report:-

(a) The Treasury Management Strategy 2013/14.

(b) The External Debt and Treasury Management Prudential Indicators and Limits for 2013/14 to 2015/16.

(c) The Investment Strategy 2013/14.

(d) The Minimum Revenue Provision (MRP) Statement included in section D which sets out the Authority's policy on MRP.

TREASURY MANAGEMENT STRATEGY

110. The suggested strategy for 2013/14 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

111. Short term rates are expected to remain on hold for a considerable time. Growth prospects are weak and consumer spending, the usual driving force of recovery, is likely to remain under pressure due to consumers focusing on repayment of personal debt, inflation eroding disposable income, general malaise about the economy and employment fears. US fiscal tightening and continuing Eurozone problems will also depress UK growth and UK deficit reduction plans may slip. The Monetary Policy Committee (MPC) is expected to hold bank rate at 0.5% throughout 2013/14.

112. Longer term fixed interest borrowing rates are based on central government borrowing costs i.e. UK gilt yields. Gilt yields will continue to be suppressed by investor concerns over Euro zone sovereign debt, decelerating activity and demand for safe haven instruments. However, the longer run trend is for gilt yields and PWLB rates to rise due to the high volume of gilt issuance in the UK and the high volume of debt issuance in other major western countries. Other risks that would push rates higher include higher inflation, improved prospects of a return to economic growth and the possibility of a UK credit rating downgrade. Whilst very difficult to predict, the effect would be upward pressure on long term rates and longer-term Public Works Loans Board (PWLB) rates could rise by around 0.25% in 2013/14.

113. The overall structure of interest rates is expected to remain the same and short term rates will continue to be lower than long term rates and are likely to remain so throughout 2013/14. In this scenario, the strategy will be to reduce investments and borrow for short periods and possibly at variable rates when required.

CAPITAL BORROWING AND DEBT RESCHEDULING

114. The borrowing requirement comprises the expected movements in the Capital Financing Requirement and reserves plus any maturing debt which will need to be re-financed. The Authority does not envisage that any new long term borrowing will be required in 2013/14. Given the likely structure of interest rates described above, it is envisaged that any borrowing to meet short term cash flow shortages will be for very short periods. Against this background, Treasury Officers will monitor the interest rate market and adopt a pragmatic approach to any changing circumstances.

115. Rescheduling 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.

116. Current PWLB lending terms have severely constrained the option to generate savings via debt rescheduling. A significant rise in long term interest rates is required before rescheduling of debt is viable. However, interest rate structures will be continually monitored for opportunities to generate savings from debt rescheduling. Any rescheduling that takes place will be reported to Members in monitoring reports.

ANNUAL INVESTMENT STRATEGY

117. The primary purpose of the Annual Investment Strategy is to set out the policies for managing investments giving priority to the security and liquidity of the Authority's investments. It also contains the policy on the use of credit ratings and credit ratings agencies, procedures for determining and limiting the use of higher risk investments and the use of external advisors.

118. 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.

119. 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

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

(a) The investment is denominated in sterling and any payments or repayments in respect of the investment are payable in sterling only.
(b) The investment is not a long-term investment (has a maturity of less than one year).
(e) The investment does not involve the acquisition of share capital or loan capital in any body corporate.
(f) 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 with the UK Government or a local Authority or a parish or community Authority.

Specified investments will comprise the following institutions: -

- The UK Government (such as the Debt Management Account deposit facility, UK Treasury Bills or a Gilt with less than one year to maturity).
- Supranational bonds of less than one year's duration*.
- UK Local Authorities.
- Money Market Funds.
- UK Banks.
- Foreign banks registered in the UK.
- Building Societies.

**(Supranational bonds represent the debt of international organizations such as the World Bank, the International Monetary Fund, regional multilateral development banks and others)*

Credit Rating Criteria

121. The Authority will invest with UK institutions or non-UK institutions that are domiciled in a country which has a minimum Sovereign long term rating of “AA”. The institution must have a high credit rating assigned by any of the three credit ratings agencies (Fitch, Moodys and Standard & Poors). To be deemed highly rated the institution must satisfy at least the minimum of the following Fitch (or equivalent) criteria:

Long term credit rating A-

If any of the agencies assigns a rating lower than the Fitch minimum (or equivalent) to an institution then the Authority will not invest with that institution.

122. In addition, the Authority will use institutions that are part nationalised UK banks.

123. Regardless of the credit rating assigned to an institution or whether it is covered by a guarantee, if any doubt over its financial standing exists then that institution is removed immediately from the counterparty lending list.

Investment Limits

124. The credit ratings and individual limits for each institution within the categories of investments to be used by the Authority in 2013/14 are as follows:

UK Government (including gilts and the DMADF)	Unlimited
UK Local Authorities (each)	Unlimited
Part Nationalised UK banks	£4m
Money Market Funds (AAA rated)	£3m
UK Banks and Building Societies (A- or higher rated)	£2m
Foreign banks registered in the UK (A or higher rated)	£2m

125. No limits on investments with the UK Government and Local Authorities have been set because they are considered to be of the highest credit quality and are essentially risk free. The limits placed on other categories reflect some uncertainty and marginally higher risk profile of the institutions within those categories. The status of part nationalized banks is unlikely to change for at least 5 and probably 10 years but there is an element of uncertainty about their status. Money Market Funds although AAA rated, invest in a diverse portfolio so are not completely risk free and have been assigned a lower limit. There is a slightly higher risk for A- rated banks as described in para 29 below and so these institutions have the lowest limit.

126. 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 Deputy Chief Executive or Treasury Manager.

Non-Specified Investments

127. Non-specified investments do not, by definition, meet the requirements of a specified investment. The Department of Communities & Local Government (CLG) guidance requires that greater detail is provided of the intended use of non-specified investments due to greater potential risk. The following types of non-specified investments may be used.

128. Deposits with the Authority's own banker shall be unlimited for transactional purposes and to allow for unusual cash flow circumstances.

129. Deposits with a maturity of greater than one year (including forward deals in excess of one year from inception to repayment) with any bank or building society that meets the credit rating criteria above.

130. Building societies which do not meet the normal credit criteria but are one of the top ten building societies, determined by asset size. Those societies that are within the top ten but do not have an agency determined credit rating shall have an individual limit of £1m. Building Society rankings are checked annually with the Building Societies Association.

Risk Management of Investment Counterparties

131. Bank and Money Market Fund ratings are checked daily. 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.

132. Credit ratings are only the starting point when considering credit risk. The Code of Practice requires the Authority to supplement credit rating information with additional operational market information which will be applied before making any specific investment decision from the agreed pool of counterparties. Credit Default Swaps and negative rating watches/outlooks are examined and the financial press, internet and financial information systems are monitored for market information regarding its counterparties. It also receives daily e-mails from various market participants that could identify potential problems. Any information that casts doubt on an institution's creditworthiness is acted on by suspending investment with that institution.

Liquidity of Investments

133. Each investment decision is made with regard to cash flow requirements resulting in a range of maturity periods within the investment portfolio. 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

Risk Benchmarking

134. The CIPFA Codes and the CLG Investment Guidance recommend the consideration and approval of security and liquidity benchmarks. Yield benchmarks are currently widely used to assess investment performance.

Security and liquidity benchmarks are new requirements although the application of these is more subjective in nature. The benchmarks are simple guides to maximum risk and so may be breached from time to time depending on movements in interest rates and counterparty criteria. The purpose of them is for officers to monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the Mid-Year or Annual Report.

135. Security: - Security is currently evidenced by the application of minimum credit quality criteria to investment counterparties, primarily through the use of credit ratings. A method to benchmark security risk is to assess the historic level of default against the minimum criteria used in the Authority's investment strategy. The Authority's minimum credit rating criteria is "A-". The average expectation of default for a one year investment in a counterparty with an "A-" long term rating is 0.09% of the total investment. The inclusion of unrated Building Societies raises this factor to 0.14% e.g. for a £1m investment the average loss would be £1,400. This is only an average and any specific counterparty loss is likely to be higher but these figures do act as a proxy benchmark for risk across the portfolio. The Authority's maximum security risk benchmark of 0.14% is embodied in the criteria for selecting cash investment counterparties and will be monitored and reported to Members.

136. Liquidity: - The Authority seeks to maintain liquid short term deposits of at least £1 million available daily.

137. Yield: - The Authority's benchmark for investment returns is the 7 day LIBID rate.

Reporting Arrangements

138. The Investments Strategy forms part of the Treasury Management Strategy which is referred to the Audit Sub-Committee for monitoring. An interim report is produced during the year and a final annual report by 30th September following the end of a financial year.

EXTERNAL DEBT PRUDENTIAL INDICATORS:

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

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

Authorised Limit

140. 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 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.

141. The authorised limits reflect the Authority's Capital Financing Requirement, identified in its capital expenditure and financing plans. They are consistent with the Treasury Management Policy Statement and Practices. The limit will ensure that total gross debt does not exceed the total of the CFR in the preceding, current or following two financial years. The Authority is asked to approve the limits below and to delegate authority to the Deputy Chief Executive, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities. In order to ensure the Authority's debt interest payments are as minimal as possible the Deputy Chief Executive is looking at options for rescheduling current debt. This may require the need to borrow at low interest rates in advance of the repayment of higher interest rate loans. To allow scope for this potential temporary increase in debt, in advance of the planned loan repayments, an additional +£20m has been included in the Authorised Limit totals. However the "true" net figure is within the reported CFR figure (£58m).

Authorised Limit for External Debt		**2013/14**	**2014/15**	**2015/16**
		£'000	**£'000**	**£'000**
Borrowing		80,000	78,000	77,000
Other Long Term Liabilities		2,000	2,000	2,000
TOTAL		**82,000**	**80,000**	**79,000**

Operational Boundary

142. 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 Deputy Chief Executive, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities.

Operational B oundary for External Debt		**2013/14**	**2014/15**	**2015/16**
		£'000	**£'000**	**£'000**
Borrowing		46,000	44,000	43,000
Other Long Term Liabilities		2,000	2,000	2,000
TOTAL		**48,000**	**46,000**	**45,000**

Actual External Debt

143. 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 £45.1 million at 31st March 2013.

TREASURY MANAGEMENT INDICATORS:

144. 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

145. 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 I nterest Rate Exposures		**2012/13**	**2013/14**	**2014/15**
		%	**%**	**%**
Fixed		100	100	100
Variable		50	50	50

146. This means that the Deputy Chief Executive will manage fixed interest rate exposures within the range 50% to 100% and variable interest rate exposures within the range 0% to 50% for 2013/14.

Maturity Structure of Borrowing

147. 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	80%	0%
12 months and within 24 months	50%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	50%	0%
10 years and above	80%	0%

Total Principal Sums Invested For Periods Longer Than 364 Days

148. It is recommended that the limit for investments of longer than 364 days be set at £2million for each of the years 2013/14, 2014/15 and 2015/16.

PERFORMANCE INDICATORS

149. 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.

150. 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.

Investments – Internal returns compared to the 7 day LIBID rate.

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

TREASURY MANAGEMENT ADVISERS

151. 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.

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

(G) REVENUE FORECASTS

153. The Authority has in recent years maintained robust medium term financial plans.

154. This plan is fully reviewed on an annual basis and monitored quarterly. This section of the report will develop a financial forecast for the Authority based upon the latest information. It will:-

- Make underlying assumptions to support the forecast,
- Discuss the key pressures that contribute to forecast deficits.

Members will recall that in the past few years the Authority's budget forecasts have dealt with significant financial challenges because of government decisions about the funding of Firefighters pensions and the poor outcomes of the Comprehensive Spending Review 2007. The Authority has made innovative changes and efficiencies to tackle the deficits, totalling nearly £11m over the 2006/07 – 2010/11 period. These savings all have been fully implemented.

155. The Authority did very badly in terms of the CSR2010 and received in excess of a 13% cut in its grant between 2011/12 and 2012/13 requiring £9.2m of savings to balance the budget for this period (subject to key budget assumptions remaining valid). However, the Government had advised fire authorities that the largest cut- back in grant would be back loaded into 2013/14 & 2014/15, and potentially be double the level in the first two years of the CSR2010 period.

156. A two phase approach was approved by the Authority which adopted the following structure:-

(a) **Phase 1; 2011 – 2013 – Years 1 &2**
Implement a £9.2m robust savings plan for 2011/12 and 2012/13 which would balance the budget, subject to key budget assumptions remaining consistent with the plan, and

(b) **Phase 2; 2013-2015 - Years 3 & 4**
Adopt a lobbying strategy for 2013/14 and 2014/15 (in conjunction with other Metropolitan Fire and Rescue Services) with a view to minimising the level of grant cuts. Depending upon the success of that lobby the Authority would face a stark choice between severe service reductions or large-scale local taxation increases. The Authority would have to (in conjunction with the community) choose its strategy between taxation and cuts.

Phase 1 Saving Options – Is the Service on Target?

157. As the table overleaf shows the Authority has made good progress in delivering its Phase one budget and is on target to deliver the required savings. However it should be noted that:-

- Savings in firefighter costs are only delivered at the rate of natural turnover through retirement and will not be fully achieved until the end of the current financial year.

- Assumed Pay Bill Freeze 2012/13. The approved budget assumed a three year pay bill freeze that in 2012/13 would save the Authority £1.000m. However firefighters and control staff received a 1% pay increase with effect from July 2012. The full year cost of this award is estimated at £0.400m. This variation to the plan will be considered as part of the budget challenge for phase 2 2013/14. Sufficient cash savings have been made in 2012/13 to cover the cost of the pay award in that year.

- Revised Duty System at Whiston – members considered report CFO/091/12 at the Authority meeting on 3rd July 2012, and approved in principle the creation of a combined blue light centre at Prescot, with the two pump fire station element to replace the one pump stations at Huyton and Whiston. Although the scheme is unlikely to reach fruition until late 2014 the required savings of £0.300m will be delivered in any case (in cash terms) as firefighter retirements continue in line with that expected. This is expected to be achieved late this year.

- Outsourced Estates function - Final Tender documents were sent to the remaining 5 bidders on the 18th July 2012. The next step is an open day with potential bidders to outline the service's needs. The process has been deferred slightly because of :-

  (a) Internal restructuring of the cleaning services team, which are already delivering permanent savings of £0.1m per annum.

  (b) The volume of building work especially in relation to Joint Control.

  The required savings of £0.250m will be delivered in any case as Estates staff have taken up voluntary severance during the year and sufficient green book savings have been made to ensure that in cash terms the saving has and will be delivered until the revised service deliver proposal can be formally implemented.

Progress in allocating out Phase 1 Approved Saving Options				
	2012/13	**2013/14**	**2014/15**	**2015/16**
	£'000	**£'000**	**£'000**	**£'000**
2011/12 Approved Savings:	**-8,525**	**-9,200**	**-9,200**	**-9,200**
Complete:				
Assume Pay Bill Freeze 2010/11	-1,000	-1,000	-1,000	-1,000
Assume Pay Bill Freeze 2011/12	-1,000	-1,000	-1,000	-1,000
Assume Pay Bill Freeze 2012/13	-1,000	-1,000	-1,000	-1,000
Reduction in Support Service Costs	-1,300	-1,300	-1,300	-1,300
Review of Capital Programme Financing	-400	-400	-400	-400
Rephasing of Vehicles Capital Programme	-100	-100	-100	-100
Manage dynamic reserve more effectively	-2,300	-2,950	-2,950	-2,950
Reduce Senior Management Costs	-400	-400	-400	-400
MACC Review	-400	-400	-400	-400
Flexible Shift Patterns at Marine 1	-75	-100	-100	-100
	-7,975	-8,650	-8,650	-8,650
Approved Saving Options yet to be finalised:				
Outsource Estates function	-250	-250	-250	-250
Flexible Shift Patterns at Whiston	-300	-300	-300	-300
	-550	-550	-550	-550
TOTAL	-8,525	-9,200	-9,200	-9,200

Note: The approved plan has earmarked the use of reserves to offset the fact that the full savings required for Phase 1 (2011/12 – 2012/13) will not be fully delivered until 2013/14 as they reflect the expected retirement profile of firefighter posts that will be deleted. This has enabled the Authority to adhere to its policy of seeking to avoid compulsory redundancies in Phase 1.

158. Therefore the Authority's Phase 1 financial plan has remained on track and the challenge ahead relates to the impact of any funding shortages in 2013/14 onwards. The following paragraphs outline;
- the assumptions made in determining the 2013/14 – 2017/18 forecasts in the latest financial plan, and
- the impact of the Government's grant settlement for 2013/14 and indicative allocation for 2014/15.

Budget Assumptions

159. The key technical and policy assumptions in the current and proposed updated financial plan are:-

Inflation & Pay Changes

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

- With effect from 2013/14 an annual increase in the paybill of 2% - It is assumed that long term pay awards will fall in line with HMT expectations of inflation
- All Other Price Inflation 2% p.a.

161. As an indicator to Members and a guide in assessing the volatility of inflation estimates - a movement of 1% in paybill inflation equates to approximately £0.5m in a full year. A 2% budgetary inflationary provision equates to approximately £1.0m in a full year for pay, and about £0.4m for price costs per annum

162. Members will recall that the Government has repeatedly emphasised the need in the current economic climate to manage public sector pay expectations. The Government has announced that it has assumed a future pay increase cap in the public sector, after the current two year pay freeze, of 1%.

163. The Government is also concerned about the cost of public pensions and has finalised the proposals on changes to firefighter and local government pension schemes (LGPS). At this time the assumption is that the pension changes will have no impact on the employer's pension costs, however;

- work is on-going with CLG to determine if any future adjustment to employers firefighter pension rates is likely, but no outcome from this review is expected for some time, and
- the Merseyside LGPS 3 year actuarial review has commenced in 2013 and will determine if any adjustment is required to the MFRA employers rate with effect from 01.04.14. The proposed financial plan assumes no change to the current rate.

Therefore the financial plan assumes that the employer's pension contribution rate to all pension schemes will continue at current rates.

The baseline financial forecast is based upon historic assumptions. The Deputy Chief Executive has reviewed the underlying inflation assumptions in order to identify savings, this is considered in Section (H).

Cost of Capital Borrowing

164. The revenue impacts of capital investment decisions and the agreed 2013/14 – 2017/18 capital programme are included within forecasts. This includes additional new start schemes of net +£0.386m. The plan also takes into account the proposed MRP policy discussed previously in section D.

Resources Available

165. The two main sources of Authority funding in the past have been Council Tax Precept (33%) and Government Formula Grant (66%). The Government has carried out a local government resource review and as a result it has introduced a new funding system for local government with effect from 2013/14 based on a "business rates retention scheme". However, in order to stick to the Government's public sector spending plans, the Government has ultimately built into the system a process to maintain local government support at levels anticipated in the 2010 CSR over the 2013/14 – 2014/15 period.

166. Under the new funding system MFRA will receive revenue support grant (RSG) and a business rates top-up grant that together with CLG's estimates local business rates share for the Authority will form what was effectively in the previous grant regime the "formula grant" funding. To help explain the level of the movement in Government funding in comparison to previous years and the existing financial plan, this report will refer to the Government support under the new retained business rate funding as "formula grant" to help explain any variations in 2013/14 and future years Government support.

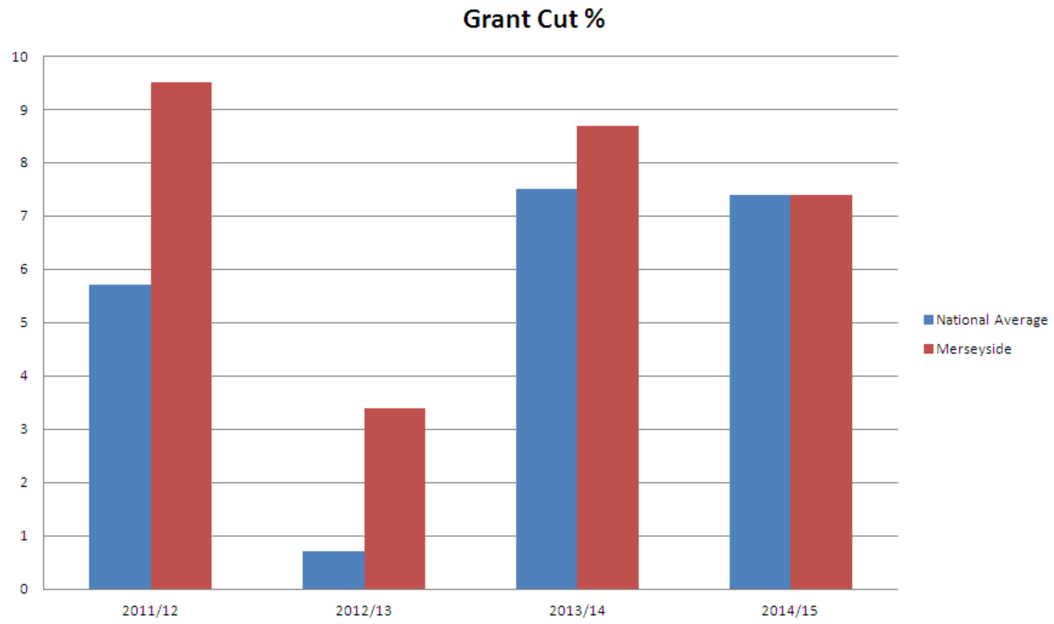
(a) Government "Formula Grant";

Central Government's has previously announced that fire authorities face a 25% real terms reduction in Government funding (equivalent to a cash reduction on the 2010/11 figure of 18%) over the 2011/12 – 2014/15 period.

The Government have stated the reduction will be back loaded for fire, with approximately one third of the reduction being phased in the first 2 financial years, (2011/12 – 2012/13) and the remainder in the last 2 years.

The Authority received a cash reduction in its grant of in excess of 13% (£7.7m) in 2011/12 – 2012/13 alone. There was significant variation between fire authorities in how the cuts were allocated in the first two years. Merseyside was cut 2.2 times as badly as the national average grant cut of 6%. Some Authorities received a grant increase.

Following the announcement of the financial settlement for 2013/14 and 2014/15 (indicative) the cuts for the fire and rescue service are still being applied at the national level as expected. The national average cut for 2013/14 is about 7.5%. However, **Merseyside Fire Authority still did worse than the national average in 2013/14 and got an 8.7% grant cut. Its grant cut for 2014/15 will be a further 7.5%.** The graph below compares the Fire Authority to national average figures for fire across the four year spending review period. This equates to approximately a £6.3m grant loss on the 2012/13 figure.



Overall Merseyside's grant has been cut 26% in cash terms compared to a national average grant cut of 19.9% over the four year period.

The Government has announced that the current austerity period is now likely to continue beyond 2014/15 and it is likely similar level of grant cuts to those in 2011/12 – 2014/15 will occur in future years. The financial forecast assumes this will be the case and a reduction of 5% to 6% in "formula grant" will be made in 2015/16 and 2016/17.

Business Rates; The new funding regime assumes each billing authority will generate a certain amount of business rates and this income yield will be split (in terms of Merseyside);

- 50% Central Government share
- 49% Billing Authority (local share)
- 1% MFRA (local share)

As Merseyside authorities collect less local business rates than the Government's "baseline funding" level each authority will receive a "top-up" business rates grant. For MFRA this equates to £10.696m (within the formula grant proportion, £13.5m after taking into account non-formula grant additions). The amount of business rates anticipated to be collected by the Merseyside billing authorities and passed to MFRA as our local share by CLG is £4.069m in 2013/14. Each billing authority has forecast their anticipated business rates and this has increased this figure by £0.015m. Therefore the financial plan assumes an MFRA local business rates yield of £4.082m in 2013/14.

It has been assumed "top up" and local share will increase by inflation after 2014/15.

(b) 2011/12 Council Tax freeze grant, £0.681m

Central Government offered all authorities a grant if they agreed to freeze the council tax in 2011/12. The Government has made this funding available for the full CSR2010 period (2011/12 – 2014/15), and as the Authority approved a Council Tax freeze in 2011/12 it was therefore entitled to grant. The financial plan assumes this funding will not continue after 2014/15.

(c) Council Tax /Precept;

Precept Increase:

The forecast budget assumes council tax increases at a level of 2.00% in 2013/14 & 2014/15, resulting in an additional precept yield of £0.443m in 2013/14 rising to £0.996m (cumulative impact) by 2014/15.

Council Tax Support Implications;

The Government has changed the way it funds the "council tax benefit subsidy" from 2013/14 that has impacted on the way billing authorities calculate the Council Tax Base;

- In effect those in receipt of support are now no longer included in the tax base calculation and therefore areas like Merseyside have significantly reduced the tax base. In 2012/13 the tax base was 422,815 and in 2013/14 it is 329,224, a reduction of 93,591 (22%), or a loss in precept income of £6.304m.

- In addition the Government cut the level of grant funding for the new council tax support system that has resulted in the need to charge a proportion of the council tax to groups on low incomes that previously paid no council tax. This is likely to result in an increase in the level of non-collection of council tax.

- The Government has made available a council tax support grant to cover those in receipt of support and therefore no longer on the tax base, for MFRA in 2013/14 this grant was £6.392m. However, after 2013/14 £3.838m of this grant will be incorporated into the "formula grant" allocation and subject to any future Government grant adjustments, (the balance £2.554m will be included within the business rates baseline allocation).

The financial plan has now been adjusted to reflect the lower tax bases from 2013/14 and this will impact on the additional precept income yield that the Authority can generate.

Previously a 1% council tax increase was estimated to generate approximately £0.280m, now it is £0.222m.

Other Assumptions

167. The Medium Term Financial Plan assumes that:-

New Dimensions Grant

168. The Authority received a grant of £1.0m in each year for crewing New Dimensions Vehicles from CLG. The financial plan assumes this grant will continue in 2013/14 – 2017/18.

Tax Base & Collection Fund changes

169. Council Tax Base; The Districts of Merseyside have set their tax bases 2013/14 and they are shown in the table below:-

District	2012/13 Council Tax Taxbase	2013/14 Council Tax Taxbase	Variance	
	£	£	£	%
LIVERPOOL	125,249.00	88,777.98	-36,471.02	-29.12%
WIRRAL	106,058.00	87,116.40	-18,941.60	-17.86%
ST.HELENS	56,135.00	46,240.00	-9,895.00	-17.63%
SEFTON	93,119.58	76,516.20	-16,603.38	-17.83%
KNOWSLEY	42,253.00	30,573.00	-11,680.00	-27.64%
	422,814.58	329,223.58	-93,591.00	-22.14%
2012/13 Band D Tax Level	67.36	67.36		
Total Income £	28,480,790	22,176,500	-6,304,290	-22.14%

170. The total tax base for the Authority has reduced by 22.14%, as a consequence of the new council tax support system, this means that each £1 of Council Tax the level of income will be significantly lower than that generated in 2012/13 by £93,591. The result of this is that the income from the current level of Council Tax is anticipated to lower by £6,304,290 without any precept increase being applied (this is assumed to be a permanent reduction). However the Government's council tax support grant does, in 2013/14, compensate the Authority for this reduction that is due to the technical change in the way the tax base is calculated. The 2013/14 Council Tax support "grant" is £6.392m

171. This means that the income forecast from a 1% increase in Council Tax in 2013/14 is now £0.222m.

Surplus and Deficit on Collection Funds

172. 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 surplus of £55,185. This impact is a one-off.

District	2013/14 Coll fund deficit / (surplus)
	£
LIVERPOOL	-119,173
WIRRAL	0
ST.HELENS	17,994
SEFTON	45,994
KNOWSLEY	0
	-55,185

The overall forecast of the deficit based upon these assumptions is shown in the table overleaf:

2013/14 - 2017/18 FINANCIAL PLAN					
	2013/14	**2014/15**	**2015/16**	**2016/17**	**2017/18**
	£'000	**£'000**	£'000	£'000	£'000
NET EXPENDITURE:					
2013/2014 Financial Plan	**71,846**	**74,410**	**76,265**	**78,075**	**79,775**
FUNDING					
Government Funding					
RSG Grant	-22,194	-18,900	-17,790	-16,681	-17,014
Business Rates:					
Local Business Rate Share	-4,069	-4,194	-4,278	-4,363	-4,451
Top Up Grant	-10,696	-11,111	-11,333	-11,560	-11,791
Formula Funding Grant settlement	-36,959	-34,205	-33,401	-32,604	-33,256
Council Tax Support Grant	-6,392	-6,392	-6,200	-6,018	-6,087
2011/12 Ctax Freeze Grant	-681	-681			
Start-Up Allocation; Government & Business Rates Funding	-44,032	-41,278	-39,601	-38,622	-39,343
Business Rates: Increase in local forecast	-15				
Council Tax -					
2012/13 Revised base	-22,176	-22,619	-23,072	-23,995	-24,955
Assume 2% rise 2013/14 & 2014/15, 4% therefafter	-443	-453	-923	-960	-998
Collection Fund (surplus)/deficit	-55				
Forecast Council Tax Income	-22,674	-23,072	-23,995	-24,955	-25,953
Updated Income Forecast	**-66,721**	**-64,350**	**-63,596**	**-63,577**	**-65,296**
Forecast Net Position (surplus) / deficit	**5,125**	**10,060**	**12,669**	**14,498**	**14,479**

The current budget therefore indicates a £5.125m deficit, rising to £10.060m by 2014/15.

Whilst there is considerable uncertainty about the detailed position beyond 2015/16 (and there will be a spending review to finalise that position), the Government has been very clear that there will be ongoing cuts in public spending until 2017/18.

Whilst Members may take a view that there is the possibility of affecting potential cuts for 2015/16 onward through a lobbying strategy, the Deputy Chief Executive would strongly recommend that the Authority needs to develop a comprehensive plan to deal with the full year deficit – since the budgetary position to that point seems to be confirmed and unlikely to change.

(H) Options for Tackling the Financial Challenge

173. The Authority has agreed a number of Value For Money Principles that have underpinned its approach to budgets and financial plans in recent years. During 2012/13 the principles were reviewed and updated to better reflect the challenges facing the Authority now and in the future. They are:-

Budget Principles

Principle 1 – Allocate resources in a way that contributes towards the achievement of MFRA's Mission, Aims and Values

Principle 2 – To continue to seek to avoid compulsory redundancy (if possible given the difficult financial circumstances)

Principle 3 – To choose budget options which minimises negative impact on the front line services or on firefighter safety

Principle 4 – To consider budget approaches which ensure the right balance between local and national funding levels and considers the views of local people on the right level of council tax balanced against aspirations for service levels

Principle 5 – To allocate resources having considered the impact on our diverse communities and our employees.

174. In applying these principles the Authority has already made largescale budgetary changes and savings. As it faces up to its biggest ever financial challenge the Authority has very limited room for manoeuvre and these principles will be difficult to maintain.

175. In considering the financial position the Authority will note that it has already approved a balanced financial plan for 2011/12 – 2012/13, ("Phase 1"). Therefore this section concentrates on how the financial challenge of £5.125m rising to £10.060m, see section G of this report, for 2013/14 – 2014/15 can be met.

Council Tax

176. The Financial Plan assumes a 2% increase for 2013/14 and 2014/15, which is the maximum assumed level before holding a referendum. The Authority might consider :-

(a) A higher Council Tax increase and holding a referendum

The level of financial challenge assumes that the Authority agrees to increase its 2013/14 precept by 2%, however, members may choose to increase the precept by more than. This would require the Authority to hold a referendum (local vote on its proposals). There are a number of practical issues relating to a potential referendum that would make it a risky proposition;

i. The Authority has to meet the costs of the referendum (Estimate £1-2m),
ii. The Authority would have to meet the cost of rebilling if it were not successful (forecast at £2m) and would still have to find the required savings to balance the budget,
iii. There are administrative limitations on the process and campaigning around any referendum

(b) <u>Freezing the Council Tax</u>

2013/14 Council Tax freeze grant, Potential £0.285m* (based on 2012/13 tax base, likely to be reduced to £0.221m);
The Government have announced the availability of a 2013/14 Council Tax freeze grant if authorities agree to freeze their Council Tax for 2013/14 at 2012/13 levels. This would be available for two years in 2013/14 & 2014/15.

The financial plan **assumes** the precept will increase by 2% in 2013/14. If, however, the Authority decided to freeze the council tax and accept the grant it would make the financial forecast worse than that set out in this report by:-

The savings considered in this report exclude any increase in precept greater than that allowed without a referendum, however each additional 1% increase would generate approximately £0.222m for the service.

<u>Budget Options – Work Undertaken</u>

177. The Authority had agreed a two phased strategy for dealing with the financial challenges following the unprecedented Government grant reductions in CSR2010. For Phase 2 (2013/14 – 2014/15) the Service would continue with the strategy of strong and direct lobbying aimed at minimising the level of grant cuts but also that the Authority instructed officers to commence work on establishing saving proposals to balance the financial plan by:-

a) The CFO to undertake a fundamental review of fire cover
b) The CFO to review the standards of fire cover appropriate for the county based upon risk
c) The CFO and management team to report back on what savings can be delivered from a fundamental review of cuts achievable in support services.
d) The Deputy Chief Executive to review the reserves strategy, the debt portfolio, alternative financing methods and the capital programme to identify any possible savings in the costs of debt servicing for the Authority
e) The Deputy Chief Executive to review in detail all technical assumptions in the base budget to assist the Authority to consider if there is any flexibility in those assumptions
f) The CFO to consult with the community of Merseyside on their view as to the potential consequences on the community of Merseyside of the potential cuts and whether they would be supportive of paying relatively small amounts of additional council tax to safeguard their Fire and Rescue Service
g) Grants delegated power to the CFO to continue to use VER/VS to reduce staff numbers where a business case exists to do so in line with the policies and procedures previously agreed by the Authority.

h) The CFO to review the current Home Fire Safety Check strategy with a view to ensuring that the investment offers the best returns in community safety.

178. The Authority was supported by local MP's, other fire authorities, councillors and partners who supported its lobbying campaign against the unfairness of Government cuts. However whilst the lobbying was to some extent successful the Authority still suffered further grant cuts of 8.7% in 2013/14 and a forecast of a 7.5% cut in 2014/15: This is a total 26% cut in grant funding over the spending review period and is higher than the national average. Significant savings will therefore be required.

OPTIONS

Back Office and Support Services

179. The table below summarises total savings of £7m.

No	Option	£'m
1	**Overachieved Savings** The Authority has overachieved in savings delivery of its Phase one plan against a £9.2m total saving target . Members might utilise that saving to support the financial plan	0.670
2	**Pay Bill Assumptions** The forecast contains an assumption that the total paybill increase will be 2% per annum. Members may take a view that it is likely that there will be further pay restraint for staff for the next two years in light of Government assumptions and comments from Treasury Ministers. Assuming a further two years of pay restraint for all staff and reducing the provision for pay bill increase to 1%- saving £1.0million. There are significant risks associated with this approach (even at a 2% level) and the DCE recommends holding specific reserves for the short term to cover any pay increases higher than this recognising that in the medium term yet more savings will be required if this is the case. Pay bill includes employer pension contributions and national insurance contributions that may also vary.	1.000
3	**Review of Inflation provision** The DCE has reviewed the baseline provision for inflation in the financial plan to reflect the 'downsizing ' of the budget which means many budgets can be cash limited as volumes of expenditure reduce. The cumulative impact of this applied over several years is significant	£1.500
4	**Review of Capital Programme** Taking account of the capital grant received from government, rephasing of the capital programme, reviewing investment income, the ability to restructure debt and reviewing asset expenditure profiles down to reflect the likely future position of the service has allowed the DCE to identify savings in the capital programme revenue costs	£1.000

5	**Income Generation** Officers have reviewed in detail the opportunities for generating extra income from service areas and have idenfied an additional £0.5m in total from:- e) PFI Fire station use by the ambulance service f) Increased efficiency through the JCC g) Shared services at the vehicle workshops h) Cost recovery of smoke alarms from low risk households	£0.500
6.	**Review of Support Services** A fundamental review of all support services has been undertaken and is reported elsewhere on the agenda.(CFO/026/13). It should be noted that this puts at least 57 non-uniform posts at risk of redundancy and that many of the "support service" areas and posts affected in fact provide front line services to the community of Merseyside notably prevention and protection	£2.307
7	**Members Allowances** Members have already committed to reducing the overall cost of members allowances by 10%	£0.020

Overall these savings will take two years to deliver

Operational Response Review

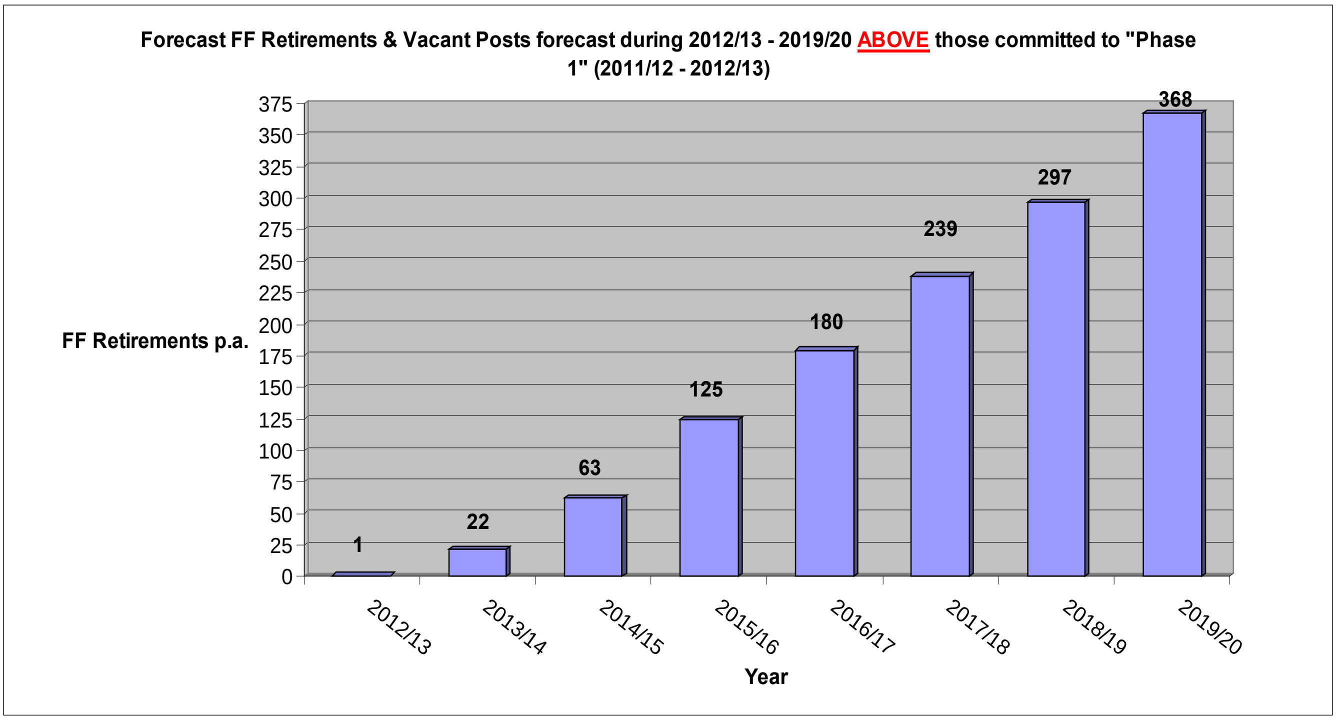
180. The CFO has carried out a fundamental review of fire cover, which is elsewhere on the Agenda (CFO/027/13), and has identified savings that will deliver a cut of £3m. This translates to a reduction of 90 fire-fighter posts and a 33% cut in the number of appliances available from the beginning of the spending review from 42 to 28.

181. The CFO recognises how important to the local community and all stakeholders the Service's Community Fire Stations are. The CFO is therefore committed to seeking to maintain that resource and keep all its fire stations open as far as practical recognising at the same time that that comes at a cost.

182. In order to mitigate the impact of this level of resource reduction on the preventative resources available to Merseyside and the essential training time reductions which might be critical for Firefighter safety, the CFO is recommending that changes be made to shift patterns and work routines that will minimise the impact on service delivery.

183. It will take over three years to deliver these front line savings from natural firefighter turnover. The table below highlights firefighter retirements over the next few years. The CFO will therefore need to manage staff dynamically within the new fire cover model to deliver the savings and efficiencies in a timely and

risk minimising way and to report back appropriately to the Authority on progress made.



184. Members will in addition note that beyond 2015/16 the number of retirements accelerates significantly. In fact more than two thirds of the firefighting workforce are in their final ten years of service. Therefore whilst cash savings are required there is also a need to undertake a significant recruitment drive in the medium term. There is a significant risk if this is not managed effectively since a large amount of experience will clearly be lost. An approach around this using reserves is discussed in more detail in the reserves section.

185. The table overleaf summarises the proposed saving options for the 2013/14 financial plan;

2013/14 - 2017/18					
	2013/14	2014/15	2015/16	2016/17	2017/18
	£'000	£'000	£'000	£'000	£'000
Forecast Net Position (surplus) / deficit	**5,125**	**10,060**	**12,669**	**14,498**	**14,479**
PHASE 2 Savings:					
Technical					
Reduce PAY inflation assumption in 2013/14 from 2 to 1 %	-400	-500	-500	-500	-500
Reduce PAY inflation assumption in 2014/15 from 2 to 1 %		-400	-500	-500	-500
Inflation Provision Review	-1,000	-1,300	-1,425	-1,500	-1,500
Capital Programme/Funding Changes assumption over availble fire capital grant on MRP/Interset;	-1,000	-1,000	-1,000	-1,000	-1,000
Phase 1 additional savings to date on Mgt/Support & other	-670	-670	-670	-670	-670
	-3,070	-3,870	-4,095	-4,170	-4,170
Income					
Joint Control Room		-200	-200	-200	-200
Income PFI Stations	-75	-100	-100	-100	-100
Workshops		-100	-100	-100	-100
Smoke Alarm	-100	-100	-100	-100	-100
	-175	-500	-500	-500	-500
Phase 2 Proposed Cuts in Support Savings	-1,675	-2,157	-2,307	-2,307	-2,407
Phase 2 Proposed Cuts in Front Line Savings	-305	-1,750	-3,100	-3,100	-3,100
SMG Contingency Reserve	100				
Use of Smoothing Reserve		-1,783			
Savings	-5,125	-10,060	-10,002	-10,077	-10,177
PHASE 3 (2015/16 ONWARDS)					
Savings yet to be identified			-2,667	-4,421	-4,302
Forecast Position	0	0	0	0	0

(I) ADEQUACY OF RESERVES AND BALANCES

Responsibilities of Chief Finance Officers

186. 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:

- the robustness of the estimates made for the purposes of determining its Budget Requirement for the forthcoming year;
- the adequacy of the proposed financial reserves.

187. 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.

188. In the Fire Authority the Chief Finance Officer is the Deputy Chief Executive – Kieran Timmins. For the purposes of the Act the "financial reserves" of the Authority would incorporate Earmarked Reserves and Working Balances.

189. 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

190. 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.

Adequacy of proposed Financial Reserves

191. 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.

192. 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.

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

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

195. A pilot Comprehensive Performance Assessment (CPA) performance indicator relating to the level of general fund reserves indicated that;

- *an appropriate level of was 5% of the forecast Net Operating Expenditure….* **Or;**
- *that the organisation had a financial risk management process operating which justified a lower level of reserves….”.*

This is for ‘normal’ rule for multi-service local authorities.

196. For this Authority a 5% forecast Net Operating Expenditure equates to approximately £3million.

However:-

(a) The Authority’s risk management arrangements have improved. As part of this budget process the Deputy Chief Executive 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.

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

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

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

(e) 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.

Current Reserves

197. In The latest financial review identifies the Authority's forecast reserves as:

Forecast Reserves 31.03.13

	Closing Balance
Earmarked Reserves	**£'000**
Spate / Other Emergencies	
Ill Health Reserve	244
Bellwin Reserve	147
Insurance Reserve	620
Emergency planning Reserve	75
Smoothing Reserve	1,495
Specific Projects	
Regional Reserve	100
Health & Safety Reserve	81
Equipment Reserve	253
Contestable Research Fund	25
Training Reserve	285
PFI Annuity Reserve	590
FSD Reserve	35
Job Evaluation Reserve	230
Healthy Living / Olympic Legacy	61
Severance Reserve	1,812
Inflation Reserve	2,000
Capital Investment Reserve	5,236
	13,289
Ringfenced Reserves	
F.R.E.E. Reserve	35
Princes Trust Reserve	134
Community Youth Team Reserve	54
Beacon Peer Project Reserve	49
Innovation Fund Reserve	144
Regional Control Reserve	18
St Helens District Reserve	8
New Dimensions Reserve	466
	908
Qtr 3 contribution to Reserves	**2,500**
Total Earmarked Reserves	**16,697**
General Fund	**4,684**
Total Reserves	**21,381**

198. In total there are resources of £21.4m. However, of this figure £6.5million relates to grant related or contractually committed projects.

Proposed Strategy

199. The Budget set by members will identify a financial strategy that in the medium term, 2013/14 – 2014/15, balances the anticipated financial position over this period. The proposed plan is based upon the key assumptions around changes to grant, pay, tax and pension costs. The Deputy Chief Executive has reviewed the risks to these assumptions and others contained within the Authority Risk Register and considered the potential cost of the financial risks. In addition some savings will take time to deliver (based on seeking to avoid compulsory

redundancy of support staff, if possible, and that operational savings reflect the expected firefighter retirements profile).

200. In light of the risks within the financial plan and the risk register the Deputy Chief Executive recommends the reserves as set out below be approved as part of the Authority's financial plan;

Reserve Heading	£'m	Comment
Increase Insurance / Catastrophe Reserve	**1.0**	In light of outstanding risks such as MMI claims, ill health retirement penalties and the need for resources to cope with any major or protracted incident.
Inflation & Pensions	**1.5**	In light of risk around 1% pay bill assumption for 2013/14 - 2014/15 a short term reserve will allow time to make the required permanent saving.
Capital Investment	**2.0**	Likely future investment in station; vehicle; ICT and other infrastructure to further modernise the service in light of future financial challenge and associated risk
Cost Smoothing	**5.5**	In order to facilitate the planned phasing of savings the financial plan requires at least £1.8m from this reserve in 2014/15. Further drawdowns are expected in 2015/16 & future years to allow the Service time to deliver additional savings.
Recruitment	**1.0**	Over the next decade almost two thirds of its firefighters are expected to retire. In addition it takes almost a year to train a firefighter across the full range of competencies. In order to meet this challenge in a prudent and structured fashion a reserve of £1m to support some staff recruitment to manage effectively succession planning is recommended
Severance	**1.0**	On the basis the Authority wishes the CFO to use every available measure and management tool to avoid compulsory redundancy and therefore it grants delegated power to reopen and utilise the Voluntary Severance / Voluntary Early Retirement programme in line with the broad framework agreed by the Authority previously
	12.0	
General Fund	**2.9**	It is normally expected that a General Fund reserve of 5% of net operating expenditure should be maintained by an organisation.but this might vary based on individual risks and earmarked reserves available. For MFRA this would be £3.4m. However, as the significant risks are known and are being managed or have a specific reserve, officers recommend maintaining a GF of £2.9m
	14.9	

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

201. Members need to consider their strategy on reserves and balances in the light of the guidance from the Deputy Chief Executive.

Budget Timetable

202. There is a legal requirement for the Authority to set a balanced budget and decide its level of precept **before** 1st March 2013.

Equality & Diversity Implications

203. The financial plan makes provision for 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.

204. Equality Impact Assessments have been prepared for the support service proposals, operational review of response within the IRMP report, and review and council tax increase proposal, copies of which are on this agenda.

Staff Implications

205. These are considered in detail in the reports on support service savings and operational response elsewhere on the agenda.

Legal Implications

206. The Authority must set a balanced budget and decide its level of precept **before** 1st March 2013.

Financial Implications & Value for Money

207. See Executive Summary.

Health & Safety and Environmental Implications

208. The budget and capital investment programme make large-scale investments in staff Health and Safety.

Contribution to Achieving the Mission

209. To Achieve; Safer Stronger Communities - Safe Effective Firefighters. The proposed financial plan considers how best to allocate resources and deliver a balanced budget in light of the approved mission of the service and service priorities.

BACKGROUND PAPERS

Report CFO/033/12 “Merseyside Fire & Rescue Authority Budget & Financial Plan 2012/2013 – 2016/2017” Authority 16 February 2012.

Report CFO/024/13 “Financial Review Report 2012/13 April to December Review” Authority 26 February 2013

Report CFO/026/13 “Support Services Review” Authority 26 February 2013

Report CFO/027/13 “Operational Response Review” Authority 26 February 2013

Report CFO/023/13 “IRMP 2013 Consultation” 26 February 2013

Glossary of Terms

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

CSR10 – Government comprehensive spending review to identify support for the public sector over 2011/12 – 2014/15 period

DCLG – Department Communities and Local Government

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

ODPM – Office of Deputy Prime Minister

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.