MERSEYSIDE FIRE AND RESCUE AUTHORITY			
MEETING OF THE:	AUDIT COMMITTEE		
DATE:	26 SEPTEMBER 2019	REPORT NO:	CFO/050/19
PRESENTING OFFICER	CHIEF FIRE OFFICER		
RESPONSIBLE OFFICER:	IAN CUMMINS	REPORT AUTHOR:	IAN CUMMINS
OFFICERS CONSULTED:	STRATEGIC LEADERSHIP TEAM		
TITLE OF REPORT:	FINANCIAL REVIEW 2019/20 - APRIL TO JUNE		

APPENDICES:	APPENDIX A1:	REVENUE BUDGET MOVEMENTS SUMMARY
	APPENDIX A2:	FIRE AND RESCUE SERVICE REVENUE BUDGET MOVEMENTS
	APPENDIX A3:	CORPORATE SERVICE REVENUE BUDGET MOVEMENTS
	APPENDIX A4:	BUDGET MOVEMENTS ON RESERVES
	APPENDIX B:	CAPITAL PROGRAMME 2019/20
	APPENDIX C:	APPROVED AUTHORITY CAPITAL PROGRAMME 2019/20 – 2023/24

Purpose of Report

1. To review the financial position, revenue and capital, for the Authority for 2019/20. The Authority receives regular comprehensive financial reviews during the year which provide a full health check on the Authority's finances. This report covers the period April to June 2019.

Recommendation

2. That Members;
   a) note the contents of the report, and
   b) approve the proposed revenue, capital and reserve budget alignments, and
   c) instruct the Director of Finance to continue to work with budget managers to maximise savings in 2019/20.

Executive Summary

Revenue:
The Authority has a detailed medium-term financial plan. The key elements of this are :-
- To control Council Tax
- To continue with its modernisation programme and deliver the Authority's Mission of achieving Safer Stronger Communities – Safe Effective Firefighters
- To deliver the required savings through efficiencies, most of which are employee related, whilst minimising the impact of the cuts.
- To release revenue savings through prudent debt management to protect/enhance frontline services

The Authority is on target to deliver the approved 2019/20 budget savings and is progressing well with the required structural changes in its workforce in order to maintain the required savings on a permanent basis.

The Authority has a strategy of maximising and delivering its savings plan as early as possible in order to fund increases in reserves or other initiatives that would act as a hedge against future financial challenges. At this point in the year this report has identified that spend is forecast to be consistent with the approved budget. Officers will continue to work through the remainder of the year to maximise any savings in order to fund an increase in the minimum revenue provision, MRP, in order to pay historic debt commitments early. By increasing the MRP payment the intention is to free-up future debt servicing revenue budget and re-invest it in frontline services or use it to meet any future financial challenges.

The total budget requirement remains at the original budget level of £60.282m. Appendix A1 – A4 outline in detail all the revenue budget and reserve movements between April and June 2019.

Capital:
The capital programme planned spend has increased by £3.823m (net), of which £3.834m relates to the re-phasing of schemes from 2018/19 into 2019/20. The revised Capital Programme is outlined in Appendix B and C.

Reserves & Balances:
The general balance remains unchanged at £2.000m. All movements in earmarked reserves are outlined in Appendix A4.

Treasury Management:
No new long term borrowing has been arranged and the Authority has continued its policy of reducing investments and only taking short term borrowing to cover cash flow requirements.

Introduction and Background

3. The purpose of this report is to enable the Authority to monitor its income and expenditure levels against its budget on a regular basis throughout the year to ensure effective financial management.

4. This report is the review of the Authority's position up to the end of June of the financial year 2019/20 (April – June 2019).

5. In order to ensure that the financial reviews provide a regular and effective financial health check on all aspects of the Authority's finances the following structure has been adopted.

Financial Review Structure	
Section	Content
A	Current Financial Year Review:- • Revenue Budget, • Capital Programme, and • Movement on Reserves
B	Treasury Management Review

(A) Current Financial Year – 2019/20

6. The purpose of the financial review report is to provide Members with an assurance that the approved budget remains robust and that the current forecast of expenditure can be contained within the available resources. If actual expenditure or income for the year is inconsistent with the current budget then the report will, if necessary, identify the appropriate corrective action.

Revenue Position:

7. Budget Movements: The attached Appendix A1 – A4 to this report summarises the movements in the revenue budget, but the following paragraphs outline the most material adjustments in the first quarter.

8. At the 2019/20 Budget Authority meeting the outcome of the 2016 firefighters pension schemes (FPS) actuarial review was not known. The advice received from the Home Office was to assume a 12.6% increase in the FPS employer rate from April 2019, and that a Home Office grant would cover 90% of the additional costs. Therefore the 2019/20 budget assumed an increase in the employer FPS on-cost of £2.800m and a grant of £2.592m. From 2020/21 the grant would be built into the Comprehensive Spending Review 2019 process and be included within the overall funding settlement grant.

9. The Home Office wrote to the Authority on 28th February to advise that the employer rate would actually be increased by 14.5% and 15.1% for the 2015 FPS and 1992 FPS respectively, resulting in an overall increase in the employer cost

of £3.360m, an additional £0.560m. The Director of Finance challenged the Home Office over the level of grant support and successfully got the Home Office / Treasury to increase the grant by £0.433m to £3.025m, (equivalent to 90% of the revised costing). Unfortunately, the increase in the FPS rate also meant that the planned £1m additional investment in frontline services approved by the Authority at its 3rd July 2019 meeting, CFO/038/19, will now require an additional £0.145m. Therefore the potential net financial impact on the budget is £0.272m (£0.560m + £0.145m less £0.433m). However, as £0.260m of the additional cost relates to the additional 0.6% increase in the FPS 1992 scheme (15.1% - 14.5%), and by 2022 the current assumption is all firefighters will be in the FPS 2015, this additional cost is only “temporary” and reducing each year. The Director of Finance, based on the latest employee spend forecast and historical spending patterns, is of the opinion that the £0.260m additional FPS 1992 employer cost can be contained within the overall employee budget. The £0.012m balance (£0.272m - £0.260m) can be met from a budget virement from the inflation contingency provision. The impact on the Medium Term Financial Plan, MTFP, (2020/21 onwards) will be dependent upon future Home Office funding continuing at the 2019/20 grant level, this will not be known until the 2020/21 Government funding support is announced (December 2019?), and any financial implications will be considered as part of the 2020/21 Budget setting process.

10. Also, there have been a number of budget adjustments with no net impact because they are either self-balancing virements within department budgets or budget increases financed by reserves in line with previously agreed Authority decisions. The budget adjustments in quarter 1 included:-

    - a virement from the inflation provision of £0.462m to cover the 2% non-uniform staff pay award and other price inflation on premises and other costs.
    - An increase of £0.445m (£0.560m + £0.145m less £0.260m for FPS 1992) in the FPS employer rate and an increase in Home Office FPS grant income of £0.433m to cover the impact of 2016 FPS actuarial review outlined in paragraphs 8 and 9 above.
    - A net contribution from reserves of £0.027m to cover planned spend on projects. The breakdown of the reserve movements are outlined in Appendix A4.

11. **The net budget requirement remains at £60.282m which is consistent with the original budget**.

12. <u>Update on Budget Savings Implementation</u>:
    All approved saving options remain consistent with the approved MTFP. The firefighter annual pay award has yet to be agreed however the offer of a 2% uplift from the employers for 2019/20 is consistent with the current financial plan’s assumption of 2%.

    The operational response savings are being delivered as expected, however the structural establishment changes required as part of the station merger initiative will not be formally implemented until the new fire station at St Helens has been built. The required firefighter saving is being delivered in cash terms as the reduction in the number of firefighters has been achieved.

13. Actual expenditure in comparison to Revenue Budget**:** The Authority is concerned that any future Government may continue to reduce the level of Government support in real terms post 2019/20. It therefore has directed the Chief Fire Officer to maximise savings in the year to accommodate options to assist with any future challenge. In recent years this meant using these savings to contribute towards the building up of reserves as a hedge against the future financial challenges or to meet one-off expenditure such as capital infrastructure investment. The current strategy is to use any additional savings to increase the planned minimum revenue provision (MRP) payment so that future debt servicing budget may be freed-up to fund the additional £1m investment in frontline services approved by the Authority.

14. After reviewing spend and income up to the end of June 2019 the expectation is that overall expenditure and income will be consistent with the approved budget:

Employee Costs;

Employee costs make-up approximately 75% of the Authority's revenue budget and is the most risk critical area of the financial plan. As a result these costs are monitored extremely closely.

Firefighter retirements have continued in line with the forecast profile adopted for the financial strategy. Non-firefighter employee costs are in line with the approved budget. At this point employee costs are expected to be in line with budgets.

However, the Government introduced changes to all public pensions in 2014 and 2015. These changes were challenged in the courts by the Fire Brigades Union (FBU) and Judges representatives as the transitional protections given to some scheme members as part of public service pensions reform was deemed discriminatory. This challenge is often referred to as the "McCloud" case. On 20th December 2018 the Court of Appeal found that these protections were unlawful on the grounds of age discrimination and could not be justified. On the 27th June 2019 the Supreme Court refused the Government the right to appeal against this decision and therefore an employee tribunal will now decide on the compensation required to redress the situation. At this point in time no indication of what the compensation agreement will be, but it has been reported that the potential national cost may be as high as £4b a year if all the public pension changes introduced were reversed.

In 2015 the employer rate for FPS 1992 was 21.7% and the new FPS 2015 14.3%. This reduction in the employer rate has been built into the approved MTFP and current budget. Any amendments to the FPS rates or compensation payments as a result of McCloud that is not funded by the Government may create a significant budget challenge for the Authority. It is unlikely any details of the proposed compensation agreement will come out before the end of the calendar or financial year, and at this point no provision has been built into the budget or MTFP to cover this issue. This matter will be considered further as part of the 2020/21 Budget setting exercise.

Contingency for 2019/20 Pay & Price Increases;

Members will recall that the budget assumed a 2% pay bill increase in 2019/20 and future years. The non-uniform staff accepted a 2% pay award for 2019/20, but the 2019/20 firefighters award has yet to be settled. The employers have offered to uplift firefighter rates by 2% for 2019/20 and the latest indication is that this may be accepted. Officers are continuing to control the allocation of non-employee inflation. In the first instance any inflationary pressure is expected to be absorbed from within the relevant budget line.

Other Non-Employee Revenue Costs;

The Director of Finance is continuing to work with budget holders to maximise savings in 2019/20. At this point in time expenditure is forecast to be in line with budgeted levels.

The Director of Finance will continue to monitor the position during the year to ensure the Service continues to deliver the required savings target and report back as the year progresses.

15. Debtor accounts under £5,000 may be written off by the Director of Finance. Five accounts have been approved for write-off under delegated powers in the first quarter following advice from litigation services totalling £1,833 plus VAT. Significant doubt existed over whether three of the special services invoices met the conditions of a chargeable service and the remaining two related to employee payments deemed non-recoverable on compassionate grounds or offsetting payments were owed to the individual.

16. <u>Summary of Revenue Forecast Position</u>: The Authority has made good progress in implementing the approved budget saving options and required organisational structure changes.

As expected the implementation of all of the approved station merger proposals have yet to be formally concluded, therefore the required budgetary structural changes remain outstanding. However, as Firefighter retirements remain as expected the Service continues to deliver in “cash” terms the required savings target.

At present, expenditure is forecast to be in line with the budget. The Director of Finance is continuing to work with budget holders to maximise savings in 2019/20 and will report in more detail in future financial reviews.

Capital Programme Position:

17. Members approved a 5 year capital programme worth £36.481m at the Authority Budget meeting on 28th February 2019, (CFO/009/19). This has now been updated for:

a) the approved 2018/19 year-end re-phasing of projects into 2019/20 of £3.834m as reported to the Policy and Resources Committee on 25th July 2018, CFO/037/19, and
b) a reduction of £0.011m in the cost of the purchase of a new a van.

18. The capital programme changes are summarised in Table below. The revised detailed capital programme is attached as Appendix B (2019/20 Capital Programme) and Appendix C (2019/20–2023/24 Capital Programme) to this report.

Movement in the 5 Year Capital Programme						
	Total Cost	2019/20	2020/21	2021/22	2022/23	2023/24
Expenditure	£'000	£'000	£'000	£'000	£'000	£'000
Amendments to Approved Schemes;						
Re-phasing of Schemes from 2018/19 into 2019/20	3,833.6	3,833.6				
Reduction in ancillary fleet	-11.0	-11.0				
	3,822.6	**3,822.6**	**0.0**	**0.0**	**0.0**	**0.0**
Funding						
Revenue Contribution to Capital Outlay(RCCO)						
Funding from Strategic Road Partnership for a van	-11.0	-11.0				
Borrowing						
Rephasing impact	3,833.6	3,833.6				
	3,822.6	**3,822.6**	**0.0**	**0.0**	**0.0**	**0.0**

Use of Reserves:

19. The analysis in Appendix A4 outlines a £4.304m drawdown from in reserves during the first quarter of 2019/20, as a result of:-
    - As part of the 2019/20 Budget the Authority approved the use of £4.277m of reserves to fund capital and other projects. This includes a net drawdown of £3.993m from the capital reserve of which most relates to the funding of the new St Helens Fire Station.
    - A further net drawdown of £0.027m in Qtr 1 to fund specific projects. .

The general revenue reserve has remained unchanged at £2.000m.

(B) Treasury Management

20. The Authority continues to "buy in" Treasury Management from Liverpool City Council. The following paragraphs reflect Treasury Management activities in the period April to June 2019.

21. **Prospects for Interest Rates;**
After the August 2018 increase in Bank Rate to 0.75%, the Bank of England Monetary Policy Committee (MPC) has put any further action on hold. Rates are not now expected to change until such time as there is greater clarity surrounding

the conclusion of the Brexit process and there is some degree of certainty of what the UK will be heading into. Bank rate forecasts of an increase of 0.25% around September 2020 are on the assumption that a form of Brexit agreement is achieved; however in the event of a no deal the MPC may well cut rates immediately by as much as 0.50%.

PWLB rates and gilt yields remain volatile and have fluctuated throughout the first quarter of 2019/20. Despite this volatility PWLB rates fell slightly for longer term loans, from 2.44% at the start of the financial year to 2.36% by the end of the first quarter.

The strategy indicated that the overall structure of interest rates whereby short term rates are lower than long term rates has continued for some time. In this scenario, the strategy would be to reduce investments and borrow for short periods and possibly at variable rates when required.

22. **Capital Borrowings and the Portfolio Strategy;**
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 2019/20. Current market conditions continue to be unfavourable for any debt rescheduling.

23. **Annual Investment Strategy;**
The investment strategy for 2019/20 set out the priorities as the security of capital and liquidity of investments. Investments are made in accordance with DCLG Guidance and CIPFA Code of Practice. Investments are made in sterling with an institution on the counterparty list.

Extreme caution has been taken in placing investments to ensure security of funds rather than rate of return. The use of deposit accounts with highly rated or nationalised banks and AAA rated money market funds has enabled reasonable returns in a low interest rate environment. In the period 1st April to 30 June 2019 the average rate of return achieved on average principal available was 0.73%. This compares with an average seven day deposit (7 day libid) rate of 0.57%.

The credit ratings and individual limits for each institution within the categories of investments to be used by the Authority in 2019/20 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
Enhanced Money Market (Cash) Funds (AAA rated)	£3m
Ultra-Short Duration Bond 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

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 Authority had investments of £22.2m as at 30th June 2019:

ANALYSIS OF INVESTMENTS END OF QUARTER 1 2019/20

Institution	Credit Rating	MM Fund*	Bank / Other	Building Society	Local Authority	Average Interest
		£	£	£	£	%
Aberdeen Global	AAA	3,000,000				0.77
Federated Investors	AAA	3,000,000				0.77
JP Morgan Sterling Liquidity Fund	AAA	3,000,000				0.66
LGIM (Legal & General)	AAA	2,200,000				0.74
Close Brothers	A		2,000,000			1.15
Goldman Sachs	A		1,000,000			1.24
Newcastle B Soc				1,000,000		0.93
Nottingham B Soc				1,000,000		0.90
Principality B Soc				1,000,000		0.96
West Bromwich B Soc				1,000,000		0.96
Highland Council					2,000,000	0.96
Lancashire CC					2,000,000	1.05
Totals		**11,200,000**	**3,000,000**	**4,000,000**	**4,000,000**	**0.92**
Total Current Investments					**22,200,000**	

**MM Fund - Money Market Funds -these are funds that spread the risk associated with investments over a wide range of credit worthy institutions.*

24. **External Debt Prudential Indicators;**
The external debt indicators of prudence for 2019/20 required by the Prudential Code were set in the strategy as follows:

Authorised limit for external debt: £70 million
Operational boundary for external debt: £59 million

Against these limits, the maximum amount of debt reached at any time in the period 1 April to 30 June 2019 was £37.6 million.

25. **Treasury Management Prudential Indicators;**
The treasury management indicators of prudence for 2019/20 required by the Prudential Code were set in the strategy as follows:

a) Interest Rate Exposures

Upper limit on fixed interest rate exposures: 100%
Upper limit on variable interest rate exposures: 50%

The maximum that was reached in the period 1 April to 30 June 2019 was as follows:

Upper limit on fixed interest rate exposures: 100%
Upper limit on variable interest rate exposures: 0%

b) Maturity Structure of Borrowing

Upper and lower limits for the maturity structure of borrowing were set and the maximum and minimum that was reached for each limit in the period 1st April to 30 June 2019 was as follows: -The treasury management indicators of prudence for 2018/19 required by the Prudential Code were set in the strategy as follows:

Interest Rate Exposures

Upper limit on fixed interest rate exposures: 100%
Upper limit on variable interest rate exposures: 50%

The maximum that was reached in the first quarter of the financial year 2018/19 was as follows:

Upper limit on fixed interest rate exposures: 100%
Upper limit on variable interest rate exposures: 0%

b) Maturity Structure of Borrowing

Upper and lower limits for the maturity structure of borrowing were set and the maximum and minimum that was reached for each limit in the period 1st April to 30 June 2019 was as follows: -

Maturity Period	Upper Limit	Lower Limit	Maximum	Minimum
Under 12 months	50%	0%	1%	1%
12 months and within 24 months	50%	0%	1%	1%
24 months and within 5 years	50%	0%	8%	8%
5 years and within 10 years	50%	0%	0%	0%
10 years and above	90%	0%	90%	90%

c) Total principal sums invested for periods longer than 364 days.

The limit for investments of longer than 364 days was set at £2 million for 2018/19. No such investments have been placed during 2019/20.

Equality and Diversity Implications

26. There are no equality and diversity implications contained within this report.

Staff Implications

27. There are no staff implications contained within this report.

Legal Implications

28. There are no legal implications directly related to this report.

Financial Implications & Value for Money

29. See Executive Summary.

Risk Management, Health & Safety, and Environmental Implications

30. There are no Risk Management, Health & Safety and Environmental implications directly related to this report.

Contribution to Our Mission: *Safer Stronger Communities – Safe Effective Firefighters*

31. The achievement of actual expenditure within the approved financial plan and delivery of the expected service outcomes is essential if the Service is to achieve the Authority's Mission.

BACKGROUND PAPERS

CFO/004/18 "MFRA Budget and Financial Plan 2019/2020-2023/2024" Authority 28th February 2019.

GLOSSARY OF TERMS