MERSEYSIDE FIRE AND RESCUE AUTHORITY			
MEETING OF THE:	POLICY AND RESOURCES COMMITTEE		
DATE:	16 DECEMBER 2021	REPORT NO:	CFO/0067/21
PRESENTING OFFICER	IAN CUMMINS		
RESPONSIBLE OFFICER:	IAN CUMMINS	REPORT AUTHOR:	IAN CUMMINS
OFFICERS CONSULTED:	STRATEGIC LEADERSHIP TEAM		
TITLE OF REPORT:	FINANCIAL REVIEW 2021/22 - JULY TO SEPTEMBER		

APPENDICES:		
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	APPENDIX A2:	FIRE AND RESCUE SERVICE REVENUE BUDGET MOVEMENTS
	APPENDIX A3:	CORPORATE SERVICE REVENUE BUDGET MOVEMENTS
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Purpose of Report

1. To review the financial position, (revenue, capital, reserves, and treasury management activities), for the Authority for 2021/22. 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 July to September 2021.

Recommendation

2. That Members;
   a. note the contents of the report;
   b. approve the proposed revenue and capital budget alignments;
   c. approve the reserve adjustments as outlined in the report, and use the £0.826m forecast favourable revenue variance to fund; and
      i. the creation of a £0.526m inflation reserve;
      ii. increase the existing pension reserve by £0.300m to cover expected additional pension administration costs.
   d. instruct the Director of Finance and Procurement to continue to work with budget managers to maximise savings in 2021/22.

Executive Summary

Revenue:
The Authority approved a five-year medium-term financial plan (MTFP) at the Budget Authority meeting on 25 February 2021. The approved MTFP delivered a balanced budget for 2021/22 based on key budget assumptions around future costs, in particular pay awards. This report updates members on the 2021/22 budget position and any issues arising in the year that may impact on the current and future years' financial position.

The Authority adopted the LGA/FBU immediate detriment framework (IDF) that allows eligible FPS pension members access to their legacy scheme benefits. The estimated additional administration and compensation costs are £0.300m over the 2021/22 – 2023/24 period.

This report identifies a net favourable variance of £0.826m, of which; £0.500m relates to a forecast underspend on employee costs; a £0.526m saving on borrowing costs; and an underachievement on income of -£0.200m.

Members are asked to approve the use of this favourable variance to;

- create an inflation reserve of £0.526m in light of increasing future pay inflation pressures, and
- increase the current pension reserve by £0.300m in light of the Authority adopting the LGA/FBU IDF.

The total budget requirement remains at the original budget level of £59.250m. Appendix A1 – A4 outline in detail all the revenue budget and reserve movements between April and September 2021.

Capital:
The capital programme planned spend has increased by £2.055m in the quarter, of which £2.000m relates to the replacement of national resilience assets and is funded by a Home Office grant. The balance, £0.055m, is for new schemes, of which £0.044m is for gas monitors and smoke blockers funded from the Grenfell infrastructure fund. The revised Capital Programme is outlined in Appendix B and C.

Reserves & Balances:
The general balance remains unchanged at £3.000m. All movements in committed 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 September of the financial year 2021/22 (April – September 2021).

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 – 2021/22

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: 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 2 included: -

- A £0.175m drawdown from the capital reserve to fund the planned implementation and development of the CFRMIS application to manage prevention and protection work streams.
- A £0.020m drawdown from the Health and Wellbeing reserve to support the LFC foundation work streams.
- Inflation provision drawdown of £0.608m to cover the firefighter annual pay award (1.5%) and other price increases.
- Increase in specific grant income to reflect the use of Grenfell protection grants (£0.297m) and apprenticeship levy funds (£0.133m) in 2021/22.

- Self-balancing virements to cover small adjustments within non-employee budget lines.

8. **The net budget requirement remains at £59.250m that is consistent with the original budget**.

9. Update on Budget Assumptions and actual expenditure:

10. The key assumptions for 2021/22 are:
    - No annual pay award in 2021/22, and
    - The McCloud pension remedy would not impact on the employer rates until 2024/25 and all other pension costs including administrating the remedy would be cost neutral, and
    - No significant unplanned growth pressures would materialise in the year,
    - Costs associated with the Covid-19 pandemic could be contained within the available resources.

11. **Annual Pay awards –** As per the last financial review report Members agreed to drawdown from the inflation and other reserves to cover;

    a) the firefighters 1.5% pay increase and increase the inflation in 2021/22 (£0.414m in 2021/22, but will rise to £0.552m in a full year), and
    b) increase the inflation provision to cover the other local government employees who have been offered 1.75%, although this has been rejected by Unison who are now consulting their members on industrial action (1.75% would cost £0.198m).

    The Authority would then consider the 2022/23 and future years funding of the 2021/22 pay awards as part of the 2022/23 budget considerations.

12. **"McCloud" remedy / Home Office Immediate Detriment offer** – The Authority approved the implementation of the LGA/FBU Immediate Detriment Framework that included retired as well as retiring eligible FPS members. As a result the additional administration and compensation costs are expected to increase compared to those for implementing the previously agreed Home Office Immediate Detriment framework (retiring FPS members only). The estimated additional costs are £0.300m over the 2021/22 – 2023/24 period. Therefore, the existing pension reserve needs to be increased by £0.300m.

13. **No significant unplanned growth pressures would materialise in the year -** The budget assumes all spending requirements can be met from the approved budget. The following paragraphs consider the September forecast outturn position and the identified variances;

14. **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.

In order to maintain the current firefighter establishment the Service has for a number of years now recruited in advance of the expected retirements. This may mean that for short periods the actual number of firefighters is slightly above the budgeted establishment. The latest September uniform employee forecast indicates a net overspend of £0.300m against the budget. However, this may reduce if retirements continue throughout the next six months and the retirements exceed the number of new recruits expected in the January 2022 in-take. The Authority has established a £2.000m recruitment reserve to cover any year-end overspend that cannot be met from other employee favourable variances.

The non-uniform establishment forecast indicates a £0.800m favourable variance due to a number of vacant posts and the fact that some employees have yet to reach the top of their budgeted grade.

Overall, the forecast variance on the total employee budget is a favourable £0.500m

15. **Non-Employee Costs;**

Capital Financing;
The current strategy is to reduce investments/internal cash and to borrow for only short periods, rather than take out new long term loans to fund capital funded through borrowing. This combined with the re-phasing of capital schemes last year, has resulted in a forecast saving on debt interest payments and the minimum revenue provision (MRP), of £0.526m.

Income;
The Authority undertakes a number of activities for which it is reliant upon external funding either through grant or fee income. The Authority has received a significant reduction in Prince's Trust funding from Wirral and St Helens colleges in 2021/22. After using the available Prince's Trust reserve and reducing costs were possible, the Service is forecasting a potential £0.050m adverse variance. At the start of the year commercial training course income was below the level assumed in the budget due to the ongoing impact of Covid, and while demand for courses has now picked-up, the anticipation is that income will be below the budgeted figure by £0.070m. Demand from other agencies for MFRS staff secondments has fallen leaving a £0.080m income shortfall. Overall, the forecast income deficit is forecast to be £0.200m. However, officers are confident income from other activities will be higher than expected by the year-end resulting in an overall balanced position.

Contingency for 2021/22 Pay & Price Increases;
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.

16. Overall the latest forecast has identified a favourable net revenue variance of £0.0826m, the table overleaf summarises the year-end forecast position based on spend to the end of September 2021:

	TOTAL BUDGET	ACTUAL as at 30.09.21	FORE-CAST	VARI-ANCE
	£'000	**£'000**	**£'000**	**£'000**
Expenditure				
Employee Costs	53,839	26,688	53,339	-500
Premises Costs	3,043	980	3,043	0
Transport Costs	7,721	3,616	7,721	0
Supplies and Services	7,091	3,472	7,091	0
Agency Services	7,217	3,130	7,217	0
Central Support Services	578	321	578	0
Capital Financing	9,884	0	9,358	-526
Income	-26,546	-18,750	-26,346	200
Net Expenditure	62,827	19,457	62,001	-826
Contingency Pay&Prices	653	0	653	0
Cost of Services	63,480	19,457	62,654	-826
Interest on Balances	-172	-43	-172	0
Movement on Reserves	-4,058	0	-4,058	0
Total Operating Cost	59,250	19,414	58,424	**-826**

17. The Director of Finance and Procurement recommends that members use the favourable variance to fund the following reserve adjustments;

- In light of the expected rise in inflation (CPI) to 4% or 5% in the coming months (before dropping down towards the Government's 2% target), that £0.526m of the favourable forecast variance be used to create an inflation reserve. The reserve would provide a temporary source of funding if future pay awards exceed the MTFP assumption (currently 2.5% p.a.).
- That the Pension reserve be increased by £0.300m in light of the expected increase in administration and compensation costs following the adoption of the LGA/FBU IDF.

Capital Programme Position:

18. The last financial review report (CFO/050/21) approved a 5-year capital programme worth £55.687m. This has now been updated for scheme additions and changes during quarter 2 of £2.055m, as outlined below:-

a) The Authority manages the national resilience asset refresh on behalf of the Home Office and receives 100% funding for the scheme. The planned programme for 2021/22 has increased by £2.000m in the quarter.
b) The Authority has received grant funding for Protection initiatives of which £0.044m has been used to purchase of gas monitors and smoke blockers.
c) New ICT hardware funded by revenue, £0.011m.
d) Re-phasing of £0.106m for the planned mini-bus replacement from 2021/22 to 2022/23.

19. The capital programme changes are summarised in Table overleaf;

Movement in the 5 Year Capital Programme						
	Total Cost	2021/22	2022/23	2023/24	2024/25	2025/26
Expenditure	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Amendments to Approved Schemes;						
National Resilience - Asset Refresh	2,000.0	2,000.0				
Ops Equip - Gas Monitors & Smoke Blockers	43.8	43.8				
Additional ICT hardware	11.6	11.6				
Re-phasing of mini buses	0.0	-105.8	105.8			
	2,055.4	**1,949.6**	**105.8**	**0.0**	**0.0**	**0.0**
Funding						
Grant						
Home Office - National Resilience Assets	2,000.0	2,000.0				
Revenue (RCCO)						
Gas Monitors & Smoke Blockers	43.8	43.8				
ICT Hardware	11.6	11.6				
Borrowing						
Re-phasing of mini buses	0.0	-105.8	105.8			
	2,055.4	**1,949.6**	**105.8**	**0.0**	**0.0**	**0.0**

20. The revised detailed capital programme is attached as Appendix B (2021/22 Capital Programme) and Appendix C (2021/22–2025/26 Capital Programme) to this report.

Use of Reserves:

21. The analysis in Appendix A4 outlines a £0.346m contribution from reserves during the second quarter of 2021/22, as a result of: -
    - A £0.150m and £0.025m drawdown from the Recruitment and Clothing reserves to cover uniform and PPE costs for the recruits.
    - A net £0.025m adjustment within the Prince's Trust reserve to reflect the fund being used to cover day-to-day revenue costs as it is no longer needed to cover a planned contribution for replacement mini-buses.
    - A £0.175m drawdown from the Capital reserve to cover planned investment in the CFRMIS prevention and protection application development.
    - A £0.020m drawdown from the Health and Wellbeing reserve to meet the planned activity with the Liverpool LFC Foundation partnership with the Service, to deliver community activities in the year.

22. As outlined in paragraph 17, and subject to Members' approval, this report recommends using the quarter 2 forecast favourable variance to: -
    - Re-create a £0.526m Inflation reserve that will be available if pay and inflation exceeds the estimates within the current MTFP. Currently the MTFP assumes future pay awards at 2.5% p.a., each 1% equates to approximately £0.500m, and
    - Increase the Pension reserve by £0.300m as the costs of administrating the LGA/FBU IDF are expected to be higher than those under the HO IDF, as they include retired eligible FPS members and compensation payments.

The general revenue reserve has remained unchanged at £3.000m.

(B) <u>Treasury Management</u>

23. The Authority continues to "buy in" Treasury Management from Liverpool City Council. The following paragraphs reflect Treasury Management activities in the period April to September 2021.

24. **Prospects for Interest Rates;**
The global economy continues to recover from the pandemic but has entered a more challenging phase. The resurgence of demand has led to the expected rise in inflationary pressure, but disrupted factors of supply are amplifying the effects, increasing the likelihood of lower growth rates ahead. This is particularly apparent in the UK due to the impact of Brexit.

While Q2 UK GDP expanded more quickly than initially thought, the 'pingdemic' and more latterly supply disruption will leave Q3 GDP broadly stagnant. The outlook also appears weaker. Household spending, the driver of the recovery to date, is under pressure from a combination of retail energy price rises, the end of government support programmes and soon, tax rises. Government spending, the other driver of recovery, will slow considerably as the economy is taken off life support.

Inflation rose to 3.2% in August. A combination of factors will drive this to over 4% in the near term. While the transitory factors affecting inflation, including the low base effect of 2020, are expected to unwind over time, the Monetary Policy Committee has recently communicated fears that these transitory factors will feed longer-term inflation expectations that require tighter monetary policy to control. This has driven interest rate expectations substantially higher.

The Bank of England (BoE) held Bank Rate at 0.10% throughout the period and maintained its Quantitative Easing programme at £895 billion, unchanged since the November 2020 meeting.

Treasury advisors now expect the Bank Rate to rise to 0.25% in Q2 2022, and believe this is driven as much by the Bank of England's desire to move from emergency levels as by fears of inflationary pressure.

Investors have priced in multiple rises in Bank Rate to 1% by 2024. However, treasury advisors believe Bank Rate will rise by a lesser extent than expected by markets.

The PWLB certainty rate for borrowing is linked to Gilt yield plus a margin of 1.00%. Gilt yields declined following the start of this financial year before rising again towards the latter end of the half year. PWLB rates for longer-term loans

have fallen slightly by 0.06% during the first half of the financial year, to 2.17% by the end of the second quarter.

The current environment remains consistent with the strategy that indicated that the overall structure of interest rates whereby short-term rates would be lower than long-term rates was expected to remain throughout 2021/22. In this scenario, the strategy was to reduce investments and borrow for short periods and possibly at variable rates when required.

25. **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 2021/22. Current market conditions continue to be unfavourable for any debt rescheduling.

26. **Annual Investment Strategy;**
The investment strategy for 2021/22 set out the priorities as the security of capital and liquidity of investments. Investments are made in accordance with DLUHC 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 July to 30 Sept 2021, the average rate of return achieved on average principal available was 0.09%. This compares with an average seven-day deposit (7-day libid) rate of -0.08%.

The credit ratings and individual limits for each institution within the categories of investments to be used by the Authority in 2021/22 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 £61.950m as at 30th September 2021, (this included a £33.8m firefighters' pension grant received on 26th July 2021 that will be utilised in the year):

ANALYSIS OF INVESTMENTS END OF QUARTER 2 2021/22

Institution	Credit Rating	MM Fund*	DMADF**	Bank / Other	Building Society	Local Authority	Average Interest
		£		£	£	£	%
Aberdeen Global	AAA	3,000,000					0.77
CCLA Investment Management	AAA	3,000,000					0.26
Debt Management Account Deposit Facility	AAA		15,000,000				0.10
Federated Investors	AAA	3,000,000					0.10
Fidelity	AAA	3,000,000					0.10
Morgan Stanley	AAA	3,000,000					0.30
HSBC (MFRS Deposit Account)	A			3,950,000			0.10
Santander	A			2,000,000			0.76
Sumitomo	A			2,000,000			0.50
Coventry BS					2,000,000		0.30
Cumberland B Soc					1,000,000		0.30
Leeds B Soc					2,000,000		0.90
Nationwide BS					2,000,000		0.30
Newcastle BS					2,000,000		0.18
Principality B Soc					1,000,000		0.60
West Bromwich BS					1,000,000		0.10
Ashford BC						2,000,000	0.30
Blackpool Council						2,000,000	0.61
City of Kingston upon Hull						3,000,000	0.36
London Fire Commissioner						2,000,000	0.80
North Lanarkshire						2,000,000	0.60
Surrey Heath BC						2,000,000	0.71
Totals		**15,000,000**	**15,000,000**	**7,950,000**	**11,000,000**	**13,000,000**	**0.41**
Total Current Investments						**61,950,000**	

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

***DMADF is an account offered by the Debt Management Office, (DMO), and is guaranteed by the UK government. The DMO is an Executive Agency of Her Majesty's Treasury. The DMO's responsibilities include debt and cash management for the UK Government, lending to local authorities and managing certain public sector funds. As the DMADF is part of HM Treasury and represent the safest counterparty the Authority can use and as such the investment limit in the strategy is unlimited.*

27. **External Debt Prudential Indicators;**
The external debt indicators of prudence for 2021/22 required by the Prudential Code were set in the strategy as follows:

Authorised limit for external debt: £62 million
Operational boundary for external debt: £57 million

Against these limits, the maximum amount of debt reached at any time in the period 1 July to 30 Sept 2021 was £36.9 million.

28. **Treasury Management Prudential Indicators;**
The treasury management indicators of prudence for 2021/22 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 July to 30 Sept 2021 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 July to 30 Sept 2021 was as follows: -

Maturity Period	Upper Limit	Lower Limit	Maximum	Minimum
Under 12 months	50%	0%	8%	8%
12 months and within 24 months	50%	0%	1%	1%
24 months and within 5 years	50%	0%	0%	0%
5 years and within 10 years	50%	0%	0%	0%
10 years and above	100%	0%	91%	91%

c) Total principal sums invested for periods longer than 365 days

The limit for investments of longer than 365 days was set at £2 million for 2021/22. No such investments were placed in the second quarter of 2021/22.

Equality and Diversity Implications

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

Staff Implications

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

Legal Implications

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

Financial Implications & Value for Money

32. See Executive Summary.

Risk Management, Health & Safety, and Environmental Implications

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

Contribution to Our Vision:	***To be the best Fire & Rescue Service in the UK.***
Our Purpose:	*Here to serve, Here to protect, Here to keep you safe.*

34. 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/010/21 "MFRA Budget and Financial Plan 2021/2022-2025/2026" Authority 25th February 2021.

CFO/050/21 "Financial Review 2021/22 – April to June" Audit Committee 28th September 2021.

GLOSSARY OF TERMS

LGA	Local Government Association
FBU	Fire Brigades Union
HO	Home Office
IDF	Immediate Detriment Framework
FPS	Fire Pension Scheme
CFRMIS	Community Fire Risk Management Information System
LFC	Liverpool Football Club