MERSEYSIDE FIRE AND RESCUE AUTHORITY

MEETING OF THE:	**AUDIT COMMITTEE**		
DATE:	**9 FEBRUARY 2023**	**REPORT NO:**	**CFO/58/22**
PRESENTING OFFICER	**IAN CUMMINS DIRECTOR OF FINANCE AND PROCUREMENT**		
RESPONSIBLE OFFICER:	**IAN CUMMINS**	**REPORT AUTHOR:**	**IAN CUMMINS**
OFFICERS CONSULTED:	**STRATEGIC LEADERSHIP TEAM**		
TITLE OF REPORT:	**FINANCIAL REVIEW 2022/23 - OCTOBER TO DECEMBER**		

APPENDICES:	**APPENDIX A1:**	**REVENUE BUDGET MOVEMENT SUMMARY**
	APPENDIX A2:	**FIRE AND RESCUE SERVICE REVENUE BUDGET MOVEMENT**
	APPENDIX A3:	**CORPORATE MANAGEMENT REVENUE BUDGET MOVEMENT**
	APPENDIX A4:	**BUDGET MOVEMENTS ON RESERVES**
	APPENDIX B:	**CAPITAL PROGRAMME 2022/23**
	APPENDIX C:	**APPROVED AUTHORITY CAPITAL PROGRAMME 2022/23 – 2026/27**

Purpose of Report

1. To review the revenue, capital, and reserves financial position for the Authority for 2022/23. 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 October to December 2022.

Recommendation

2. It is recommended that Members.
    a. note the contents of the report;
    b. approve the proposed revenue and capital budget alignments;
    c. approve the use of the £0.250m forecast favourable revenue variance to fund an increase in the Capital Reserve in order to reduce future debt servicing costs, and
    d. instruct the Director of Finance and Procurement to continue to work with budget managers to maximise savings in 2022/23.

Executive Summary

Revenue:
The Authority approved a five-year medium-term financial plan (MTFP) at the Budget Authority meeting on 24 February 2022. The approved MTFP delivered a balanced budget for 2022/23 based on key budget assumptions around costs, in particular pay. This report updates members on the 2022/23 budget position and any issues arising in the year that may impact on the future years' financial position.

The MTFP assumed a 2.5% pay award for 2022/23, but local government staff have accepted an offer of a £1,925 fixed sum for all grades. This equates to approximately a 6.5% increase on the green/red book staff employee budget, and is 4% or £0.465m above the budget assumption. The current firefighters pay offer is 5%, and the FBU is currently seeking its members' views on the offer and have recommended not to accept it. A 5% settlement would exceed the budget provision by £0.695m in 2022/23 rising to £0.926m in a full year. Members have received a number of reports on the impact of the current high energy prices and a potential increase in energy costs of +200% or £1m above the budget for 2022/23. After taking into account the Government initiative for reducing business energy costs, (October 2022 to March 2023), energy costs are now expected to exceed the current budget by £0.5m - £0.7m.

Any pay award or energy costs that cannot be contained within the budget will be funded from the £3m inflation reserve in 2022/23. The Authority will need to consider the impact of higher inflationary increases in 2022/23 as part of the 2023/24 budget process.

The total budget requirement remains at the original budget level of £61.792m. Appendix A1 – A4 outline in detail all the revenue budget and reserve movements between October and December 2022.

Capital:
The capital programme planned spend has reduced by £0.012m in the quarter and £7.608m re-phasing from 2022/23 into future years. 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 December of the financial year 2022/23 (October – December 2022).

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 – 2022/23

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 3 included:-

- An increase in the new TDA/capital reserve of £5.000m in 2022/23 to reflect the re-phasing of the scheme and spend slipping into 2023/24, when the reserve will be required.
- A planned drawdown of £0.010m from the equipment reserve to purchase supplies.
- A full breakdown of the reserve movements is outlined in Appendix A4.
- A £0.567m virement from the inflation provision to cover the "red book" staff 2022/23 pay settlement and other non-employee inflation costs including £0.118m for energy.

- The National Resilience Assurance budget has been increased by £0.294m realigned to reflect agreed Home Office spending plans, and is 100% funded by grant income.
- Other self-balancing virements to cover small adjustments within non-employee budget lines.

8. **The net budget requirement remains at £61.792m, which is consistent with the original budget**.

9. <u>Update on Budget Assumptions and forecast actual expenditure:</u>

10. The key budget assumptions for 2022/23 are:

    I. Annual pay awards of 2.5%, and
    II. General price inflation of 2% and Energy inflation of 12%,
    III. The new TDA / Station can be built within the approved budget,
    IV. No significant unplanned growth pressures would materialise in the year,

    I. **Annual Pay awards assumption**, a 2.5% pay award for 2022/23;

    The last financial review report covered the impact of the Local government staff 2022/23 pay award of £1,925 fixed sum for all grades, and this would equate to a 6.5% increase on the green book staff employee budget, 4.0% or £0.465m above the budget assumption.

    The initial firefighters pay offer was 2% and this has now been increased to 5%. If accepted this would exceed the budget by £0.695m in 2022/23 rising to £0.926m in a full year (pay award is from 1st July). At the time of writing this report the FBU has recommended rejection of the offer and is balloting its members on industrial action.

    II. **Non-pay inflation – energy;**
    Members have received a number of reports on the impact of the current high energy costs on the budget. The estimated increase in energy costs in 2022/23 was expected to be in the order of £1m above the budget. Following the Government's decision to offer some financial support to businesses from October 2022 to March 2023, the overspend is expected to be £0.5m - £0.8m.

    As a result of the higher pay and energy inflation, a potential £2m overspend against the current budget may materialise in 2022/23. In order to ensure the revenue budget remains in a balanced position throughout 2022/23, Members approved the use of the £3m inflation reserve to cover any pay award or energy costs that cannot be contained within the available budget.

    The Authority will need to consider the impact of higher 2022/23 inflation as part of the 2023/24 budget process.

III. **The new TDA / Station can be built within the approved budget;** Building work commenced in October and currently the planned scheme is expected to be built within the approved budget.

IV. **No significant unplanned growth pressures would materialise in the year -** The budget assumes all spending requirements can be met from the approved budget.

11. The following paragraphs consider the December forecast revenue outturn position and potential variances;

I. **Employee Costs**;
Employee costs make-up nearly 80% of the Authority's revenue expenditure budget (*net of revenue costs associated with capital spend*) 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 December uniform employee forecast indicates a small potential underspend of £0.200m against the budget. However, this may change as the new recruits commence their employment with the Service in January 2023, and further retirements are expected before the end of the year. The forecast doesn't include the impact of the 2022/23 firefighter pay award, as this will be covered by the inflation provision and reserve.

The non-uniform establishment forecast indicates a **£0.100m favourable variance** due to staff recruitment and retention problems.

II. **Non-Employee Costs;**
Excluding energy costs, see budget assumption section, all other spend and income is expected to be consistent with the approved budget.

III. **Interest on Balances;**
The recent increase in interest rates has meant investment income is now expected to exceed the budget, £0.172m, **by £0.150m**.

12. Overall the latest forecast has identified a favourable net revenue variance of £0.250m. The Director of Finance and Procurement would recommend that Members' approve that the £0.250m favourable variance be used to increase the Capital Investment reserve and this would then be used to reduce future capital borrowing. The table overleaf summarises the year-end forecast position based on spend to the end of December 2022:

Anticipated Year-End Revenue Position (excl. National Resilience)	TOTAL BUDGET	ACTUAL as at 31.12.22	FORE-CAST	VARI-ANCE
	£'000	£'000	£'000	£'000
Expenditure				
Employee Costs	52,664	39,205	52,564	-100
Premises Costs	3,170	2,787	3,170	0
Transport Costs	1,328	1,024	1,328	0
Supplies and Services	3,543	2,182	3,543	0
Agency Services	6,766	4,850	6,766	0
Central Support Services	640	389	640	0
Capital Financing	26,292	0	26,292	0
Income	-14,682	-12,264	-14,682	0
Net Expenditure	79,721	38,173	79,621	-100
Contingency Pay&Prices	883	0	883	0
Cost of Services	80,604	38,173	80,504	-100
Interest on Balances	-172	-287	-322	-150
Movement on Reserves	-18,640	0	-18,640	0
Total Operating Cost	61,792	37,886	61,542	**-250**

13. The Director of Finance and Procurement will continue to monitor the position during the year to look to deliver savings to contribute towards the funding of the 2022/23 pay awards and increased energy costs.

14. Debtor accounts under £5,000 may be written off by the Director of Finance and Procurement. No account was written-off under delegated powers in the first quarter.

Capital Programme Position:

15. The last financial review report (CFO/048/22) approved a 5-year capital programme worth £70.865m. This has now been updated for scheme additions and changes during quarter 3 of (£0.012m), as outlined below:-

a) Officers have reviewed the current 2022/23 programme to identify likely scheme start and completion dates and as a result identified £7.608m re-phasing into 2023/24. The most significant re-phasing is due to;

i. The new TDA and fire station is expected to be completed as planned (end of April 2024), however adverse weather and a slightly delayed starting date has meant £5.000m has been re-phased into 2023/24.Planned spend in 2022/23 is £14m.

ii. Tenders are currently being evaluated for a number of other major building refurbishment schemes and discussions are taking place with bidders to drive costs down as bids have come in higher than expected due to current price inflation in the construction market. Delays in finalising other build projects sign-off due to resources being prioritised on commencing the new TDA and other major schemes, and, the re-profiling of schemes to reflect actual lifecycle schedules has meant a further £1.110m of building work has been re-phased into 2023/24.

iii. ICT projects of £1.273m have been re-phased into 2023/24. The investment in the new command and control suite, £0.501m, is linked into the New TDA and will be phased towards the later stages of the development, although orders for equipment are expected to be placed in April 2024. Other schemes have been delayed due to delays in finalising specifications or start dates of projects have been slipped due to other priorities.

b) New ICT hardware of £0.006m has been approved and will be funded from a revenue contribution.

c) The planned replacement of ancillary vehicles has been reduced by 1 from 20 to 19 in 2024/25 following a review of service needs, saving £0.018m

16. The capital programme changes are summarised in Table below. The revised detailed capital programme is attached as Appendix B (2022/23 Capital Programme) and Appendix C (2022/23–2026/27 Capital Programme) to this report.

Movement in the 5 Year Capital Programme						
	Total Cost	2022/23	2023/24	2024/25	2025/26	2026/27
Expenditure	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Amendments to Approved Schemes;						
Qtr 3 re-phasing of schemes from 2022/23 into future years	0.0	-7,608.0	7,618.0	-10.0		
Reduction in ancillary fleet programme	-18.0			-18.0		
New ICT Hardware	5.8	5.8				
	-12.2	**-7,602.2**	**7,618.0**	**-28.0**	**0.0**	**0.0**
Funding						
Capital Reserve/ RCCO						
Re-phasing of new TDA	0.0	-5,000.0	5,000.0			
New ICT hardware	5.8	5.8				
Borrowing						
Re-phasing from 2022/23	0.0	-2,608.0	2,618.0	-10.0		
Ancillary VehiclesOperational Drones	-18.0			-18.0		
	-12.2	**-7,602.2**	**7,618.0**	**-28.0**	**0.0**	**0.0**

Use of Reserves:

17. The analysis in Appendix A4 outlines the £4.990m contribution to reserves to reflect:

a. The impact of the new TDA re-phasing and the rephrasing of the £5.000m drawdown of the TDA/Capital reserve from 2022/23 to 2023/24, and

b. The planned £0.010m drawdown from the equipment reserve in quarter 3 to fund planned operational equipment.

18. As outlined in this report any pay award settlements or energy costs that cause spend to exceed the available budget will be funded by a drawdown from the £3m inflation reserve during the year.

19. This report recommends that Members' approve the use of the £0.250m favourable variance identified in quarter 3, to fund an increase in the capital investment reserve to reduce future capital borrowing.

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

(B) Treasury Management

21. The Authority continues to "buy in" Treasury Management from Liverpool City Council. The following paragraphs reflect Treasury Management activities in the period October to December 2022.

22. **Prospects for Interest Rates;**
The conflict in Ukraine continued to keep global inflation elevated and the UK and global economic outlook remains weak. Political uncertainty in the UK improved in the later part of the period following a change in government to what financial markets perceived as being more fiscally prudent.

The economic backdrop during the April to December period continued to be characterised by high energy and commodity prices, high inflation and the associated impact on consumers' cost of living, as well as little likelihood that the Russia-Ukraine hostilities will end any time soon. China started to lift some of its zero-Covid policy restrictions at the end of the period causing a sharp increase in infections, but also leading to questions over potential under reporting of the number of cases by the Chinese government due to how it is counting the figures.

Central Bank rhetoric and action continued to remain robust. The Bank of England, Federal Reserve and the European Central Bank all increased interest rates over the period and committed to fighting inflation, even in the face of potential recessions in those regions.

UK inflation remained high, but there were tentative signs it may have peaked.

The Bank of England increased the official Bank Rate to 3.5% over the period. From 0.75% in March, the Monetary Policy Committee (MPC) pushed through rises at every subsequent meeting over the period, with outsized hikes of 50bps in August and September, 75bps in November and then another 50bps in December. The Committee noted, at its' December meeting, that domestic inflationary pressures are expected to remain strong and continuing rhetoric around combating inflation means further rate rises are predicted.
The cost of both long and short term borrowing has risen dramatically over the April – December period, with rates at the end of December around 2% - 3% higher than

those at the beginning of April. Rate rises have been driven primarily by inflation and the need for central banks to control this by raising interest rates. Particularly dramatic rises were seen in September after Liz Truss' 'mini-budget' included unfunded tax cuts and additional borrowing to fund consumer energy price subsidies: over a twenty-four-hour period some PWLB rates increased to 6%. Rates have now fallen from September peaks but remain well above recent historical norms. The PWLB 10 year maturity certainty rate stood at 4.59% at the end of 2022.

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.

23. **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 2022/23. Current market conditions continue to be unfavourable for any debt rescheduling.

24. **Annual Investment Strategy;**
The investment strategy for 2022/23 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 part-nationalised banks and AAA rated money market funds has enabled reasonable returns in a low interest rate environment. Recent increases to Bank of England base rates have also improved the prospects for investment returns. In the period 1st October to 31 December 2022 the average rate of return achieved on average principal available was 2.04%. This compares with an average SONIA rate (Sterling Overnight Rate) of 1.75%.

The credit ratings and individual limits for each institution within the categories of investments to be used by the Authority in 2022/23 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 £47.600m as at 31st December 2022, see table below:

ANALYSIS OF INVESTMENTS END OF QUARTER 3 2022/23

Institution	Credit Rating	MM Fund*	DMADF	Bank / Other	Building Society	Local Authority	Average Interest
		£		£	£	£	%
Aberdeen Liquidity	AAA	3,000,000					1.29
CCLA Investment Management	AAA	1,400,000					0.72
DGLS	AAA	3,000,000					2.07
Federated Investors UK (Overnight)	AAA	1,700,000					1.59
DMADF			12,000,000				1.95
HSBC (MFRS Deposit Account)	A			500,000			1.32
Santander	A			2,000,000			2.35
Cumberland BS					1,000,000		2.35
Leeds BS					2,000,000		2.35
Newcastle BS					1,000,000		2.35
Principality BS					1,000,000		1.55
Bradford Metropolitan DC						3,000,000	2.75
Cornwall Council						2,000,000	2.80
Lancashire CC						2,000,000	2.10
Medway Council						2,000,000	1.30
North Lanarkshire CC						2,000,000	3.90
South Cambridgeshire DC						3,000,000	1.95
Thurrock Council						3,000,000	1.88
Wyre Forest DC						2,000,000	2.00
Totals		**9,100,000**	**12,000,000**	**2,500,000**	**5,000,000**	**19,000,000**	**2.03**
Total Current Investments						**47,600,000**	

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

25. **External Debt Prudential Indicators;**
The external debt indicators of prudence for 2022/23 required by the Prudential Code were set in the strategy as follows:

Authorised limit for external debt: £73 million
Operational boundary for external debt: £56 million

Against these limits, the maximum amount of debt reached at any time in the period 1 October to 31 December 2022 was £33.7 million.

26. **Treasury Management Prudential Indicators;**
The treasury management indicators of prudence for 2022/23 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 October to 31 December 2022 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 1 October to 31 December 2022 was as follows: -

Maturity Period	Upper Limit	Lower Limit	Maximum	Minimum
Under 12 months	50%	0%	0%	0%
12 months and within 24 months	50%	0%	0%	0%
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%	100%	100%

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 2022/23. . One investment of £2m has been placed during 2022/23.

Equality and Diversity Implications

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

Staff Implications

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

Legal Implications

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

Financial Implications & Value for Money

30. See Executive Summary.

Risk Management, Health & Safety, and Environmental Implications

31. 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.

32. 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/007/22 "MFRA Budget and Financial Plan 2022/2023-2026/2027" Authority 24th February 2022.

CFO/045/22 "Financial Review 2022/23 – April to June" Audit Committee 27th September 2022.

CFO/048/22 "Financial Review 2022/23 – July to September" Policy and Resources Committee 15th December 2022.

GLOSSARY OF TERMS

MTFP Medium Term Financial Plan

TDA Training & Development Academy

GDP Gross Domestic Product

PWLB Public Works Loans Board