MERSEYSIDE FIRE AND RESCUE AUTHORITY			
MEETING OF THE:	**POLICY AND RESOURCES COMMITTEE**		
DATE:	**15 DECEMBER 2016**	**REPORT NO:**	**CFO/086/16**
PRESENTING OFFICER	**TREASURER**		
RESPONSIBLE OFFICER:	**IAN CUMMINS**	**REPORT AUTHOR:**	**IAN CUMMINS**
OFFICERS CONSULTED:			
TITLE OF REPORT:	**FINANCIAL REVIEW 2016/17 - APRIL TO SEPTEMBER**		

APPENDICES:	**APPENDIX A1:**	**REVENUE BUDGET MOVEMENTS SUMMARY**
	APPENDIX A2:	**FIRE AND RESCUE SERVICE REVENUE BUDGET MOVEMENTS SUMMARY**
	APPENDIX A3:	**AUTHORITY REVENUE BUDGET MOVEMENTS SUMMARY**
	APPENDIX A4:	**MOVEMENTS ON RESERVES**
	APPENDIX B:	**CAPITAL PROGRAMME 2016/17**
	APPENDIX C:	**APPROVED AUTHORITY CAPITAL PROGRAMME 2016/17 – 2020/21**

Purpose of Report

1. To review the financial position, revenue and capital, for the Authority for 2016/17. 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 first 6 months of the year (April – September 2016).

Recommendation

2. That Members;
   - Note the potential £0.550m favourable revenue position identified within this report,
   - Approve the utilisation of the £0.550m favourable revenue position to increase the firefighter recruitment reserve in light of the expected firefighter retirement profile and the need to recruit trainees before the establishment falls below the approved staffing level, and
   - Instruct the Treasurer to continue to work with budget managers to maximise savings in 2016/17.

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 of which most are employee related whilst minimising the impact of the cuts.

The Authority is on target to deliver the approved 2016/17 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 savings and delivering its savings plan as early as possible in order to increase reserves as a hedge against future financial challenges. Overall this report has identified that in cash terms the Authority is £0.550m ahead of its saving plan target. Members are asked to approve utilising this saving to fund an increase in the firefighter recruitment reserve in light of the expected firefighter retirement profile and the need to recruit trainees before the establishment falls below the approved staffing level. The Treasurer is continuing to work with budget holders to maximise savings in 2016/17.

The total budget requirement remains at the original budget level of £61.507m. Appendix A1 – A4 outline in detail all the revenue budget and reserve movements between April and September 2016.

Capital:
The capital programme planned spend has increased by £0.985m, of which £0.600m relates to the Authority procuring National Resilience Assets on behalf of the Home Office funded by a grant and £0.382m relates to an increase in the new Prescot fire station scheme costs. Overall the changes have resulted in no movement to the level of required borrowing within the programme. 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:
In August 2016 the Bank of England cut the base rate to 0.25%. Short-term interest rates are expected to remain at 0.25% until the end of the year. 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.

Financial Processes:
Performance in Financial processes remains strong.

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 2016/17 (April – September 2016).

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
C	Internal Audit

(A) Current Financial Year – 2016/17

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 A to this report summarises the movements in the revenue budget. The net budget requirement remains at £61.507m which is consistent with the original budget.

8. 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. Members granted delegated authority to the CFO to reach an agreement with the Home Office over MFRA taking on the role of Lead Authority for the delivery of National Resilience assurance (CFO/029/16). The agreement has now been signed-off and expenditure and grant income budget lines have been increased to reflect the receipt of a £1.275m revenue and a £0.600m capital grant to fund National Resilience related expenditure incurred on behalf of the Home Office and Fire and Rescue Service. The firefighters pay award was agreed at 1% and £0.239m was drawn down from

the inflation provision to reflect that outcome. The net use of reserves for the period was a contribution to reserves of £3.205m. The re-phasing of the spend on Saughall Massie and St Helens station new builds resulted in a reversal of the £3.728m drawdown from the capital investment reserve in 2016/17. The balance in reserve movements reflected other planned project drawdowns in the quarter.

9. **Update on Budget Savings Implementation:**
Pre-2016/17 Budget the Authority had approved savings of £25.557m as part of the 2015/16 medium term financial plans with a target of £25.297m by 2016/17. The formal completion of the station merger proposals will ensure all outstanding saving options are formally implemented and the necessary structural changes have been actioned. The operational savings will take until 2017 to deliver in full because they are being achieved by natural firefighter retirement rates. The full saving target will be delivered in cash terms as long as the retirement rate remains consistent with the current expectation.

Table A below summarises the progress in implementing the approved saving options at the time of writing this report:

Table A

Progress in Implementing 2011/12 - 2015/16 Approved Saving Options	2016/17	2017/18	2018/19	2019/20	2020/21
	£'000	£'000	£'000	£'000	£'000
A) Options formally implemented into budget	-23,541	-23,401	-23,401	-23,401	-23,401
B) Approved Saving Options yet to be formally implemented:					
Operational Response - Prescot / Saughall Massie / St Helens - but FF retirements are delivering the saving in cash terms	-1,756	-2,156	-2,156	-2,156	-2,156
Total	-25,297	-25,557	-25,557	-25,557	-25,557

Actual staff numbers are continually monitored to ensure the Service continues to deliver in "cash" terms the required saving target.

10. **The Authority approved an additional £11.0m of savings in the 2016/17 Budget Authority meeting on 25th February 2016**, to be delivered in full by 2019/20. The saving plan included;

- efficiency savings of £6.0m by reducing management and support services costs,
- a known £1.0m increase in the council tax base that the plan assumed is permanent.

Despite identifying efficiencies of £7.0m the Authority had to approve an unavoidable reduction of £4.0m from the operational front line in order to balance the financial plan by 2019/20. The operational saving has been phased so it can be achieved by firefighter anticipated retirement rates.

All saving options assumed in 2016/17 have been successfully implemented. In addition the 2016/17 staff pay awards are consistent with the 1% assumption in the plan. Progress is ongoing to deliver the future years savings.

The table below summarises the 2016/17 budget's approved saving options (£11.0m less the 2016/17 Council Tax base income increase £1.023m)

2016/17 - 2019/20 MTFP				
	2016/17	2017/18	2018/19	2019/20
	£'000	£'000	£'000	£'000
Saving Proposals:-				
Pay Strategy:				
Change **Pay Assumption from 2% to 1%** over 2016/17 - 2019/20 period	-450	-950	-1,450	-1,950
Review long term FPS Employer Budget	0	-180	-255	-375
Review NI increase following SERPS changes	0	-125	-125	-125
Council Tax – Tax Base:				
Assume increase of 0.5% in 2016/17 base from 2017/18	0	-125	-125	-125
Non-Employee and Technical saving options:				
Review Non-Employee Budgets	-350	-350	-350	-350
Review MRP payments	0	-500	-675	-825
Review Inflation for non-employee / cash limit budgets	-198	-500	-650	-728
Support Staff & Senior Management	-499	-1,249	-1,499	-1,499
Operational Response Staff Saving	0	-1,000	-2,800	-4,000
Use of Smoothing Reserve	331	-1,075	-406	0
	-1,166	-6,054	-8,335	-9,977

11. **Actual Expenditure in comparison to Revenue Budget:** The Authority is facing further grant cuts over the period 2017/18 – 2019/20 and therefore has directed the Chief Fire Officer to maximise savings in the year to contribute towards the building up of reserves. Such reserves can then be used as part of an implementation and risk management strategy to deliver savings. After reviewing spend up to the end of September 2016 Officers have identified the following savings:

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 are slightly ahead of schedule compared to the forecast profile adopted for the financial strategy. After taking account of other small employee variances on the employee budget the expected overall saving on employee costs is £0.250m, equivalent to -0.5%.

Other Non-Employee Revenue Costs;

Additional one-off savings have been identified within the Supplies and Services – minor supply budget savings in accounts such as administrative,

training, cleaning supplies, travel, subsistence and subscriptions and have contributed to a forecast saving of £0.065m.

Contingency for 2016/17 Pay & Price Increases;

All pay awards for 2016/17 have been settled and are in line with the 1% assumed in the financial plan. Officers are continuing to control the allocation of the non-employee inflation provision to determine if any efficiencies can be identified in light of the forthcoming financial challenge. At this point in time a saving of £0.235m is anticipated.

The Treasurer is continuing to work with budget holders to maximise savings in 2016/17 and will continue to monitor actual staff numbers during the year to ensure the Service continues to deliver in "cash" terms the required saving target.

Summary of Revenue Forecast Position: The Authority has made good progress in implementing the approved budget saving options and required organisational structural changes.

Overall the latest forecast has identified a revenue saving of £0.550m. Members are asked to approve the utilisation of this saving to fund an increase in the firefighter recruitment reserve in light of the expected firefighter retirement profile and the need to recruit trainees before the establishment falls below the approved staffing level (see Reserves section). Table B summarises the revenue year-end forecast position based on spend to the end of September 2016:

Table B: Anticipated Year-End Revenue Position

	FIRE SERVICE BUDGET	Fire Authority	TOTAL BUDGET	ACTUAL as at 30.09.16	FORE-CAST	VARI-ANCE
	£'000	£'000	£'000	£'000	£'000	£'000
Expenditure						
Employee Costs	46,244	401	46,645	23,441	46,395	-250
Premises Costs	2,670	0	2,670	1,065	2,670	0
Transport Costs	1,381	0	1,381	611	1,381	0
Supplies and Services	3,226	44	3,270	1,035	3,205	-65
Agency Services	5,842	0	5,842	2,861	5,842	0
Central Support Services	434	92	526	193	526	0
Capital Financing	10,488	0	10,488	0	10,488	0
Income	-6,509	0	-6,509	-2,903	-6,509	0
Net Expenditure	63,776	537	64,313	26,303	63,998	-315
Contingency Pay&Prices	703		703	0	468	-235
Cost of Services	64,479	537	65,016	26,303	64,466	-550
Interest on Balances	-372		-372	-26	-372	0
Movement on Reserves	-3,137		-3,137	0	-3,137	0
Total Operating Cost	60,970	537	61,507	26,277	60,957	-550

Capital Programme Position:

12. The last financial review report (CFO/066/165) approved a 5 year capital programme worth £41.999m. This has now been updated for scheme additions and changes during Quarter 2 of £0.985m which are summarised in the table below:

TABLE C

Movement in the 5 Year Capital Programme						
	Total Cost	2016/17	2017/18	2018/19	2019/20	2020/21
Expenditure	£'000	£'000	£'000	£'000	£'000	£'000
Amendments to Approved Schemes;						
New Prescot Fire station - increase (CFO/028/16)	382.0	382.0				
New ICT hardware funded from Revenue	2.8	2.8				
National Resilience Assets	600.0	600.0				
	984.8	**984.8**	**0.0**	**0.0**	**0.0**	**0.0**
Funding						
Borrowing:						
Capital Reserve (ICT Hardware)						
Prescot New CFS- increase (CFO/28/16)	340.0	340.0				
Prescot New CFS- Knowsley MBC to cover knotweed removal	42.0	42.0				
Revenue Contribution to Capital Outlay(RCCO)						
IT Equipment (IT003)	2.8	2.8				
Capital Grant						
National Resilience Assurance Grant	600.0	600.0				
	984.8	**984.8**	**0.0**	**0.0**	**0.0**	**0.0**

13. Although the level of planned expenditure has increased the level of required borrowing has remained the same as all the changes are funded by non-borrowing resources. Details of the planned changes in Quarter 2 are outlined below:

- Members have considered and approved the build of a new community fire station at Prescot. At the Authority meeting on 24th April 2016 report CFO/028/16 advised members of a required increase in the planned spend for this scheme. Members approved the request to increase the scheme costs from £5.350m to £7.018m for the build requirement and £0.145m for the land purchase. The additional costs were to be met from the capital investment reserve. Knowsley have now offered the land for free but the works costs have increase by £0.382m as the result of additional ground remedial works to make good the disused mineshafts and the removal of Japanese Knotweed for which Knowsley MBC have contributed £0.042m. The additional cost, £0.382m, is to be funded from external contributions of £0.042m and an increase in the drawdown from the capital investment reserve of £0.340m.
- The Home Office have asked MFRS to provide the lead on National Resilience Assurance. This responsibility includes the capital asset refresh spend, £0.600m, funded by a grant. This initiative has now been included within the capital programme.
- Additional ICT hardware funded from revenue £0.003m.

14. The revised detailed capital programme is attached as **Appendix B** (2016/17 Capital Programme) and **Appendix C** (2016/17–2020/21 Capital Programme) to this report.

Use of Reserves:

15. The analysis in Appendix A4 outlines the £3.205m movement on reserves during the second quarter of 2016/17. The net increase in reserves reflects;
    - the re-phasing of the Saughall Massie and St Helens new station build schemes into 2017/18 and therefore the drawdown of £3.728m capital reserve can be re-credited back to the reserves this year,
    - the planned use of the firefighter ill health reserve to cover £0.163m of penalty charges for ill health retirements from previous years,
    - the increase in new fire station at Prescot, £0.340m,
    - the balance, £0.020m, relates to the planned spend in specific projects carried forward from 2015/16.

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

16. The expected firefighter retirement profile will see the number of current firefighter fall from the just under 700 full time equivalents now to around 300 by 2025. It can take up to 2 years for a trainee firefighter to become competent and therefore new recruits must be taken on in advance of the establishment falling critically below the required operational staffing level. On average over the next 10 years the service is expecting around 40 firefighters to retire each year. The CFO has established a workforce planning strategic group to consider when and how many firefighters the Service needs to recruit and on what contractual basis. What is clear is that these recruits will need to be appointed before the establishment falls below the budgeted level given the numbers who are expected to leave the Service over the next 10 years. This matter will be considered in more detail during the 2017/18 budget making process but initial thoughts are that the current recruitment reserve of £1.000m, will need to be increased by between £3m - £6m. A review of the current reserves is being carried out that will hopefully see a significant contribution towards that target with the balance coming from any future revenue underspends in this and future years. It is therefore recommended that the £0.550m revenue saving identified in this report is allocated to increase the firefighter recruitment reserve.

(C) Treasury Management

17. 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 2016.

18. **Prospects For Interest Rates;**
    Business confidence endured a sharp shock and recovery following the Brexit vote in June. However it is generally anticipated that growth in the economy will be weak throughout the second half of 2016 and in 2017. The Bank of England addressed the expected slowdown in growth by a package of measures including a cut in the base rate to 0.25%. A further cut to 0.10% is anticipated before the end of the year. One off increases in inflation following a devaluation of the pound are likely to be accepted by the Bank of England with base rates not now expected to increase again until May 2018.

    There has been significant volatility in PWLB rates rising and falling as the gilt market reacted to news in the run up to the referendum. After the vote, there was a flight to

safety as equities were sold and investments transferred to gilts resulting in PWLB rates falling to historically low levels. Long term PWLB rates fell by 1% during the first half of the financial year. The prospect of further quantitative easing purchases of gilts in the coming months has continued the downward pressure on PWLB rates.

The strategy indicated that the overall structure of interest rates whereby short term rates are lower than long term rates was expected to remain throughout 2016/17. In this scenario, the strategy would be to reduce investments and borrow for short periods and possibly at variable rates when required.

19. **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 2016/17. Current market conditions continue to be unfavourable for any debt rescheduling.

20. **Annual Investment Strategy;**
The investment strategy for 2016/17 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.

The credit ratings and individual limits for each institution within the categories of investments to be used by the Authority in 2016/17 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
UK Banks and Building Societies (A- or higher rated)	£2m
Foreign banks registered in the UK (A or higher rated)	£2m

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 September 2016 the average rate of return achieved on average principal available was 0.56%. This compares with an average seven day deposit (7 day libid) rate of 0.20%.

The Authority had investments of £38.9m as at 25th September 2016, (this included a £25.8m firefighters' pension grant that will be utilised in the year). The table below outlines the breakdown of were the current investments are held:

ANALYSIS OF INVESTMENTS END OF QUARTER 2 2016/17

Institution	Credit Rating	MM Fund*	Bank / Other	Building Society
		£	£	£
Aberdeen Liquidity Fund	AAA	3,000,000		
Blackrock	AAA	3,000,000		
Deutsche/DGLS/State Street	AAA	2,500,000		
Federated Investors UK	AAA	3,000,000		
Fidelity	AAA	3,000,000		
Goldman Sachs	AAA	1,900,000		
LGIM (Legal & General)	AAA	3,000,000		
Morgan Stanley	AAA	500,000		
Standard Life Investors (Ignis)	AAA	3,000,000		
Handelsbanken Inst Access	AA		2,000,000	
HBOS 12 MTH FTD	A+		2,000,000	
HBOS 12 MTH FTD	A+		2,000,000	
Santander 365 day Notice Account	A		2,000,000	
Cumberland B Soc	Unrated			1,000,000
Nationwide B Soc	A			2,000,000
Newcastle B Soc	Unrated			1,000,000
Nottingham B Soc	Unrated			1,000,000
Principality B Soc	Unrated			1,000,000
Skipton B Soc	A-			1,000,000
West Brom B Soc	Unrated			1,000,000
Totals		**22,900,000**	**8,000,000**	**8,000,000**
Total Current Investments				**38,900,000**

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

21. **External Debt Prudential Indicators;**
The external debt indicators of prudence for 2016/17 required by the Prudential Code were set in the strategy as follows:

Authorised limit for external debt: £73 million
Operational boundary for external debt: £61 million

Against these limits, the maximum amount of debt reached at any time in the first half of the financial year 2016/17 was £60.1million.

22. **Treasury Management Prudential Indicators;**

The Treasury Management indicators of prudence for 2016/17 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 first half of the financial year 2016/17 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 first half of the financial year 2016/17 was as follows: -

Maturity Period	Upper Limit	Lower Limit	Maximum	Minimum
Under 12 months	50%	0%	5%	5%
12 months and within 24 months	50%	0%	2%	0%
24 months and within 5 years	50%	0%	3%	3%
5 years and within 10 years	50%	0%	8%	8%
10 years and above	90%	0%	84%	82%

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 2016/17. No such investments have been placed during 2016/17.

(D) Internal Audit

23. The Authority continues to "buy in" Internal Audit services from Liverpool City Council. Since the last financial review report Internal Audit have completed some audit work but the reports have yet to be agreed. Most audit work is carried out in the second part of the year to fit in with service work demands and provide relevant data for the year-end audit.

Equality and Diversity Implications

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

Staff Implications

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

Legal Implications

26. There are no legal implications contained within this report.

Financial Implications & Value for Money

27. See Executive Summary.

Risk Management, Health & Safety, and Environmental Implications

28. There are no risk management, health and safety or environmental implications contained within this report.

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

29. 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/014/15 CFO/008/16 "MFRA Budget and Financial Plan 2016/2017-2019/2020" Authority 25th February 2016.

CFO/074/15 "Financial Review 2016/17- April to June" Audit and Scrutiny Committee 15th September 2016.

GLOSSARY OF TERMS

PWLB Public Works Loans Board