MERSEYSIDE FIRE AND RESCUE AUTHORITY			
MEETING OF THE:	AUTHORITY BUDGET MEETING		
DATE:	26 FEBRUARY 2015	REPORT NO:	CFO/014/15
PRESENTING OFFICER	DEPUTY CHIEF EXECUTIVE		
RESPONSIBLE OFFICER:	KIERAN TIMMINS	REPORT AUTHOR:	IAN CUMMINS
OFFICERS CONSULTED:			
TITLE OF REPORT:	MERSEYSIDE FIRE AND RESCUE AUTHORITY BUDGET AND FINANCIAL PLAN 2015/2016 – 2019/2020		

APPENDICES:		
	APPENDIX A(1):	DRAFT SUMMARY REVENUE BUDGET ANALYSIS
	APPENDIX A(2):	DRAFT DETAILED REVENUE BUDGET ANALYSIS
	APPENDIX B:	PROPOSED CAPITAL PROGRAMME 2015/16 – 2019/20 SUMMARY
	APPENDIX B(1):	CURRENT APPROVED CAPITAL PROGRAMME 2014/15 – 2018/19
	APPENDIX B(2):	PROPOSED NEW CAPITAL SCHEMES 2015/16 – 2019/20
	APPENDIX C	2014/15 – 2015/16 APPROVED £6.300M SAVING PLAN
	APPENDIX D	2015/16 – 2019/20 MEDIUM TERM FINANCIAL PLAN

Purpose of Report

1. To present information to allow Members to set a medium term capital and revenue financial plan that allocates resources in line with the Authority's strategic aims and ensures that the Authority delivers an efficient, value for money service. This will also allow the Authority to determine a budget for 2015/16 and a precept level in line with statutory requirements.

Recommendation

2. That Members consider the report and proposed budget and:-

    a. Note the 2015/16 service budgets set out in the report.

    b. Endorse the Deputy Chief Executive's recommendation on maintaining the current level of general fund balance, £2.000m, and maintaining the reserves as outlined in Paragraph 151 to 153 of this report.

    c. Endorse their current plan to increase the precept by just below 2% for 2015/16, raising the Band D Council Tax from £70.07 to £71.47 and confirm the strategy for future precept rises (the plan assumes 2% in each

year thereafter).

d. Re-affirm the approved 2014/15 – 2015/16 £6.300m saving plan outlined in Appendix C.

e. Endorse the assumptions in developing the 2015/16 – 2019/20 Financial Plan outlined in the report and approve the Medium Term Financial Plan in Appendix D and the 2015/16 budget estimate of £62.169m.

f. Approve the capital strategy and investment strategy as summarised in Appendix B.

g. Approve the Minimum Revenue Payment (MRP) strategy for 2015/16 as outlined in Paragraph 79 of this report.

h. Note the prudential indicators relating to the proposed capital programme, paragraph 90 to 92 of this report.

i. Approve the Treasury Management Strategy outlined in Section F and agree the Treasury Management indicators set out in paragraph 97 of this report for:-

- External Debt
- Operational Boundary for Debt
- Upper limits on fixed interest rate exposure
- Upper limits on variable rate exposure
- Limits on the maturity structure of debt
- Limits on investments for more than 364 days

j. Note that recommendations above provide an approved framework within which officers undertake the day to day capital and treasury activities.

Introduction and Background

Information

3. The Authority is required to determine its budget and precept level for 2015/16 by 1st March 2015.

4. This report will present all the necessary financial information in a single report. This report considers:-

   a. Forecast Revenue Estimates
   b. The Proposed Capital Programme
   c. Savings and Growth Options
   d. The Treasury Management Strategy
   e. The Minimum Revenue Payment Policy for the Authority

5. Considering all the financial issues to be taken into account a single report ensures that the Authority can:-

   a. Consider the borrowing freedoms available under the prudential code
   b. Reflect best practice
   c. Provide value for money
   d. Focus on the link between capital investment decisions and revenue budgets
   e. Continue developing their strategic financial plan

6. The following report structure will be adopted:-

Section	Focus	Paragraph
A	Executive Summary	7-29
B	Background Information	30-49
C	Capital Programme	50-74
D	Minimum Revenue Provision Statement	75-84
E	Prudential Indicators	85-94
F	Treasury Management Strategy	95-97
G	Revenue Forecasts 2015/16 – 2019/2020	98-124
H	Options for Tackling the Financial Challenge	125-138
I	Adequacy of Reserves and Balances	139-154
J	Budget Timetable & Resolution	155-158

A) EXECUTIVE SUMMARY

7. The Authority must set a balanced budget and a precept level by 1st March 2015.

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

   Our Mission:
   To Achieve; Safer, Stronger Communities - Safe Effective Firefighters

   Our Aims:
   Excellent Operational Preparedness
   Excellent Operational Response
   Excellent Prevention and Protection
   Excellent People

9. Members will recall that they set a balanced budget and plan for two years (2014/15- 2015/16) when they set the 2014/15 budget last year. The key elements of the current plan are:-

   - A 10% reduction in support staff numbers and overall support costs by £1.5m
   - Other technical savings of £1.4m
   - Unavoidable savings in the front-line response by 4 station mergers or outright closures, and a reduction of around 90 Firefighter posts delivered by natural turnover rates, saving £3.4m

10. The Government has now announced the final settlement funding for 2015/16. The grant cut in 2015/16 is 9.1% (slightly higher than the 8.5% anticipated last year). This is a further £0.210m cash cut. However this is based upon certain assumptions about related costs and is expected to be offset by other savings in relation to the implementation of the Firefighters pension schemes although this cannot be confirmed at this time.

11. A draft 5 year financial plan has been prepared using the latest information and the following key assumptions:

    - Annual increases in council tax of (fractionally below) 2%.
    - A pay bill increase of 1% in 2015/16 and 2% thereafter. The pay bill includes all pay related costs including pension contributions and national insurance.
    - 2% per annum General Price Inflation.
    - That government funding cuts will continue beyond 2015/16 in a profile broadly similar to that which has been applied over the spending review period since all major political parties have committed to tackle the national deficit during the next parliament (although it is accepted the actual level of cuts may vary as there appear to be significant policy approach differences between the political parties).

12. The report assumes the Authority will maintain its approved two year plan (2014/15 – 2015/16) and that it will seek to lobby the Government to minimise the impact of any changes in any future Comprehensive Spending Review, but only deal with any

financial challenge once known. Therefore if the Authority set a precept increase at just below 2% (as assumed in the current plan) then no further savings would be required to set a balanced budget for just 2015/16.

The table below summarises the forecast financial plan:-

2015/16 - 2019/20 MTFP					
	2015/16	2016/17	2017/18	2018/19	2019/20
	£'000	£'000	£'000	£'000	£'000
2014/2015 Approved Financial Plan	61,113	62,889	64,589	66,089	67,589
2015/16 Issues					
Increase in Sec 31 Grant for restricted NNDR increase	-267	-77	-77	-77	-77
Minimum Revenue Provision (MRP) & Interest Payable on loans			250	500	750
Adjust Planned Drawdown from smoothing Reserve to reflect movement in Council Tax yield	1,323				
2014/15 Financial Plan Expenditure Forecast	**62,169**	**62,812**	**64,762**	**66,512**	**68,262**
FUNDING					
Government Funding - Settlement Funding Assessment	-37,004	-34,082	-31,748	-29,898	-28,447
Adjustment for Local Business Rate income forecast from Districts to CLG estimate	95	0	0	0	0
NNDR Collection Fund (surplus)/deficit	235	0	0	0	0
Council Tax -					
Base Precept Income	-23,430	-24,482	-24,972	-25,471	-25,980
Council Tax Base (increase) / decrease	-572	0	0	0	0
Assume **2% rise 2015/16 to 2019/20**	-480	-490	-499	-509	-520
Council Tax Collection Fund (surplus)/deficit	-1,013				
Updated Income Forecast	**-62,169**	**-59,054**	**-57,219**	**-55,878**	**-54,947**
Forecast Net Position (surplus) / deficit	**0**	**3,758**	**7,543**	**10,634**	**13,315**
Potential Future Saving To Be Identified	**0**	**-3,758**	**-7,543**	**-10,634**	**-13,315**

13. Section H of this report "Options for Tackling the Financial Challenge" considers what areas of the future budget could deliver the potential funding gap following next year's Comprehensive Spending review by any new government.

Reserves and Balances

14. In light of the financial risks facing the Authority it has increased reserves in recent years. The latest financial review report CFO/005/15 identifies a 2014/15 forecast revenue underspend which will allow the Authority to increase its capital investment reserve by a further £0.4m. The current estimated reserves as at 31.03.15 are:-

- Ringfenced Reserves (not available for general spend) £1.5m
- Earmarked Reserves (created to fund future projects or as a resource to meet some potential future spend) £19.6m
- General Fund Reserve (required to cover unexpected events) £2.0m

£23.1m

15. Of the £19.6m of earmarked reserves, £14.2m of this has already been committed to fund future capital investment including the construction of new stations, and therefore avoiding additional borrowing. The remaining £5.4m earmarked reserves are:-

	£'m
Severance Reserve	0.6
Recruitment Reserve	1.0
Firefighter Safety	0.8
Inflation Reserve	1.1
Ill Health Cost	0.4
Equality / DDA	0.2
Insurance and Catastrophe	1.1
Other	0.2
	5.4

16. As previously stated this report identifies a number of potential risks in relation to the key assumptions in the medium term financial plan. If any of these assumptions vary then the forecast balanced budget position will be affected. Any resultant material deficit might result in the Authority having difficulty in maintaining its value for money principles and in particular avoiding compulsory redundancies.

17. The Deputy Chief Executive recommends the Authority hold the £5.4m identified above in reserves at the start of the financial plan. More information on reserves is set out in section (I).

18. Members should be mindful that reserves, balances and one-off savings should only be used to finance one-off expenditure. If such monies are used to fund ongoing revenue expenditure without taking action to reduce underlying expenditure, the Authority would find itself facing the same deficit in the next and future years but without reserves available to finance it. This is underlined by the District Auditor's 'Golden Rule' - that "one off" revenue reserves should not be used to support 'ongoing' revenue expenditure.

Council Tax Increase

19. The proposed financial plan assumes a (just below) 2% council tax increase in 2015/16 and each year thereafter.

20. The Authority may choose to use a further precept increase to bridge the gap, however current legislation requires that any increase above a threshold set by the Secretary of State must be subject to a referendum of the electorate of Merseyside. Any vote against such an increase will require a revised budget and incur the expense of re-billing all the districts within Merseyside. For 2015/16 any proposed increase at or in excess of 2% or more will require such a referendum.

21. Alternatively the Authority might take-up the option of the council tax freeze grant in 2015/16. A (just below) 2% increase in the precept would yield £0.480m and a 1% council tax freeze grant is £0.298m, a variance of £0.182m.

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

Council Tax Increase			
	0%	2%	Change
Band D Tax	70.07	71.47	1.40
District Precept	£m	£m	£m
LIVERPOOL	6.6188	6.7510	0.1322
WIRRAL	6.2604	6.3855	0.1251
ST.HELENS	3.3499	3.4168	0.0669
SEFTON	5.4878	5.5975	0.1097
KNOWSLEY	2.2855	2.3311	0.0456
	24.0024	24.4819	0.4795
Council Tax Freeze Grant			0.2980
Additional Income IF precept increased by 2%			0.1815

Capital

23. The proposed 5 year capital programme is detailed in section C. The table below summarises the proposed investments which are mainly in the Authority's property, vehicle and ICT assets which total nearly £27.3m across the life of the programme.

Proposed Authority Capital Programme for 2015/2016 - 2019/2020

Capital Expenditure	Total Cost £	2015/16 £	2016/17 £	2017/18 £	2018/19 £	2019/20 £
Building/Land - current	**10,946,500**	9,366,000	455,500	352,000	396,500	376,500
Fire Safety - current	**3,877,000**	777,000	775,000	775,000	775,000	775,000
ICT - current	**3,071,000**	737,000	531,000	556,000	816,000	431,000
Operational Equipment & Hydrants - current	**1,837,000**	225,000	168,000	525,000	484,000	435,000
Vehicles - current	**7,536,100**	2,675,100	1,526,000	1,228,000	858,000	1,249,000
Ependiture	**27,267,600**	**13,780,100**	**3,455,500**	**3,436,000**	**3,329,500**	**3,266,500**
Financing Available	**Total £**	**2015/16 £**	**2016/17 £**	**2017/18 £**	**2018/19 £**	**2018/19 £**
Capital Receipts						
Sale of 2 existing N-le-W LLAR properties		275,000				
Sale of Huyton FS (CFO/095/14)			250,000			
Sale of Whiston FS (CFO/095/14)			250,000			
	775,000	275,000	500,000	0	0	0
Revenue Contribution to Capital Outlay (RCCO)						
CFS alarm installation (salaries)		450,000	450,000	450,000	450,000	450,000
CFS alarm installation (Income from FSD)		50,000	50,000	50,000	50,000	0
	2,450,000	500,000	500,000	500,000	500,000	450,000
Capital Reserve						
Prescot FS New Build (CFO/095/14)		830,000				
	830,000	830,000	0	0	0	0
Grants						
Prescot FS New Build (CFO/095/14)		1,770,000				
	1,770,000	1,770,000	0	0	0	0
Total Non Borrowing	**5,825,000**	**3,375,000**	**1,000,000**	**500,000**	**500,000**	**450,000**
Unsupported Borrowing	**21,442,600**	**10,405,100**	**2,455,500**	**2,936,000**	**2,829,500**	**2,816,500**
Total Funding	**27,267,600**	**13,780,100**	**3,455,500**	**3,436,000**	**3,329,500**	**3,266,500**

24. This capital programme has a borrowing requirement of £10.405 million in 2015/16 and £21.443 million across the whole life of the plan. The proposed borrowing is unsupported borrowing or prudential as Members will note that the Government no longer allocates any supported borrowing to FRA's and therefore no longer builds any revenue grant funding support for new borrowing in the formula grant. This means all borrowing is prudential. At present only those fire station mergers approved following public consultation are included in the capital programme, (currently just the Prescot proposal).

25. The Authority needs to be mindful of the revenue costs of borrowing. Current and future debt servicing costs as a consequence of the proposed capital programme have been built into the proposed financial plan. This report provides members with a number of prudential indicators so they can ensure that this commitment is considered affordable, prudent and sustainable in light of these prudential indicators (Section E).

Treasury Management

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

27. The proposed strategy is set out in Section F and includes limits for the next three years on:-
    - Overall Level of External Debt
    - Operational Boundary for Debt
    - Upper limits on fixed interest rate exposure
    - Upper limits on variable rate exposure
    - Limits on the maturity structure of debt
    - Limits on investments for more than 364 days

Minimum Revenue Payment (MRP) Statement

28. MRP is the amount of money set aside in the revenue budget by the Authority each year to reduce its overall level of debt. The Authority is required under the new Local Authorities (Capital Finance and Accounting, England, Amendment) Regulations 2008 to prepare a statement on its policy for MRP in respect of the forthcoming year. Regulations require the Authority to pay debt at a rate which it considers prudent.

29. The Deputy Chief Executive has reviewed the MRP policy in line with the legislation and the report outlines the proposed MRP policy for 2015/16 and future years.

B) BACKGROUND INFORMATION

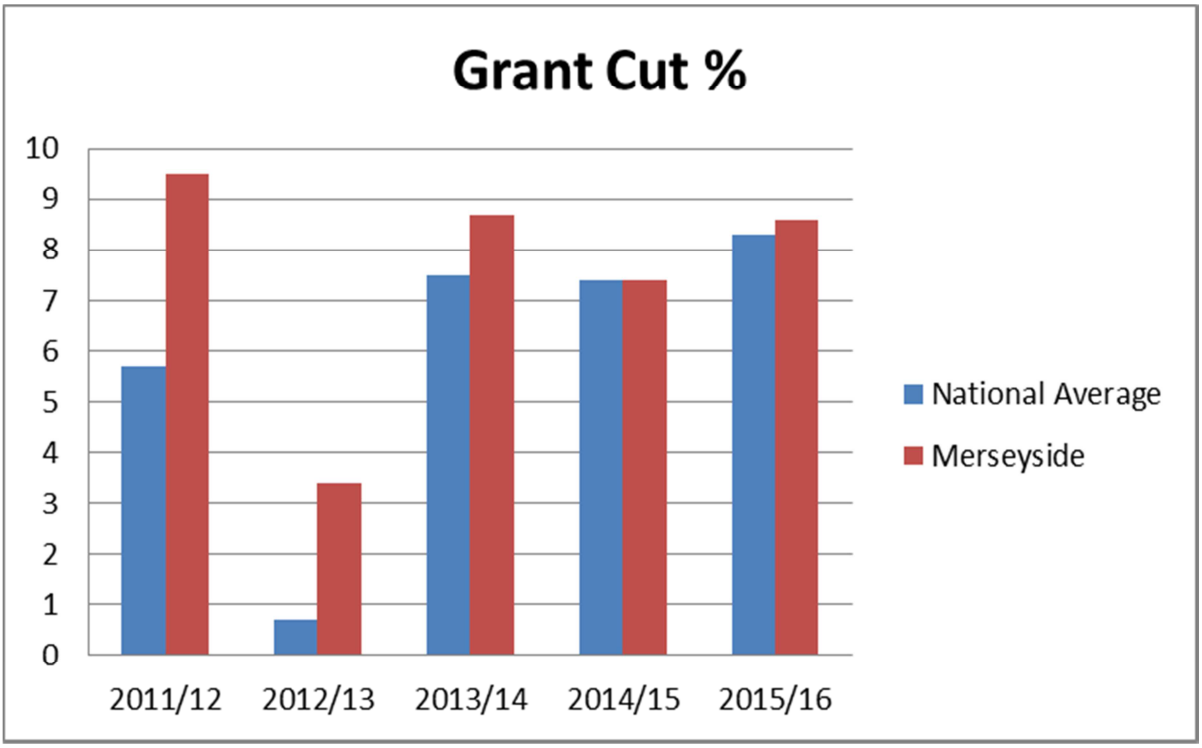
30. This section provides general financial information on the Authority's finances and financial health.

Corporate Strategy

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

32. For many years now the Authority has maintained a comprehensive five year financial plan and capital programme. In 2010 the new Government announced its austerity plan in an attempt to reduce national debt, a significant element of the plan was to reduce the level of government funding for local government including fire and rescue.

33. The cumulative percentage reduction in grant for Merseyside between 2011/12 and 2015/16 equates to a 33% reduction, compared to a national average grant cut of 26% over the four year period for stand-alone Fire and Rescue Authorities, as shown in the table below:



34. The Authority has already approved plans to deal with the cuts up to 2015/16.

35. The Integrated Risk Management Plan (IRMP) is the key driver in the allocation of the Authority's resources in response to the risks facing Merseyside.

36. The Authority's IRMP states the main strategic themes that the Authority has been progressing and its plans for the future. The 2013/16 IRMP was agreed in June 2013 and elsewhere on this agenda a supplement provides an update for 2015/16.

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

Our Mission;

To Achieve; Safer Stronger Communities - Safe Effective Firefighters

Our Aims;

Excellent Operational Preparedness

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

Excellent Operational Response

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

Excellent Prevention and Protection

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

Excellent People

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

Is the Overall Strategy Working?

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

- Being the first FRA's in the UK to visit 100,000 households in a single year to carry out Home Fire safety Checks (approximately 700,000 HFSC's in total have been carried out).
- Fitting approximately 850,000 smoke alarms.
- Significantly reducing the impact of antisocial behaviour during the bonfire period through effective joint working with partners.
- Reducing fire deaths from an average of 20 in 1999 to an average of 8 over the last ten years, (a 50% reduction).
- Reduced the total number of all types of fires and their impacts.

39. The table below summarises performance over the last decade:

Year	Accidental Dwelling Fires	Injuries in Accidental Dwelling Fires	Fatalities in Accidental Dwelling Fires	Anti Social Behaviour Fires
2004-2005	1470	173	11	12258
2005-2006	1456	155	11	11689
2006-2007	1336	126	8	12721
2007-2008	1286	69	9	10449
2008-2009	1302	107	9	7648
2009-2010	1299	117	8	7394
2010-2011	1199	137	5	6893
2011–2012	1196	131	5	6088
2012-2013	1136	128	6	3903
2013-2014	1153	126	8	5141
2014-2015 Q3	768	94	6	3303
Reduction between 2004/05 - 2013/14	-21.56%	-27.17%	-27.27%	-58.06%

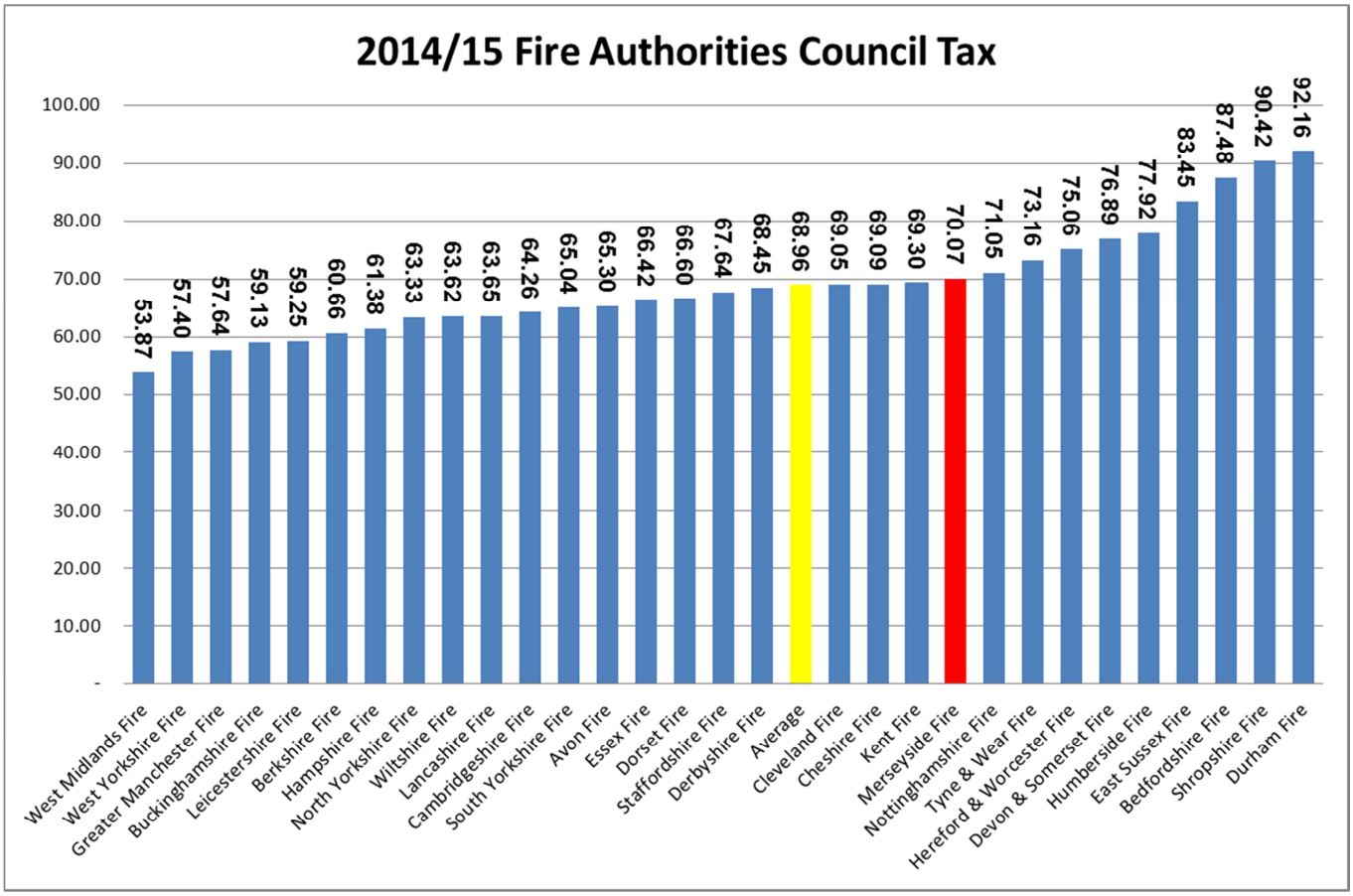
Financial Strategy and where are we now?

40. In recent years the Authority has adopted a financial strategy that:-

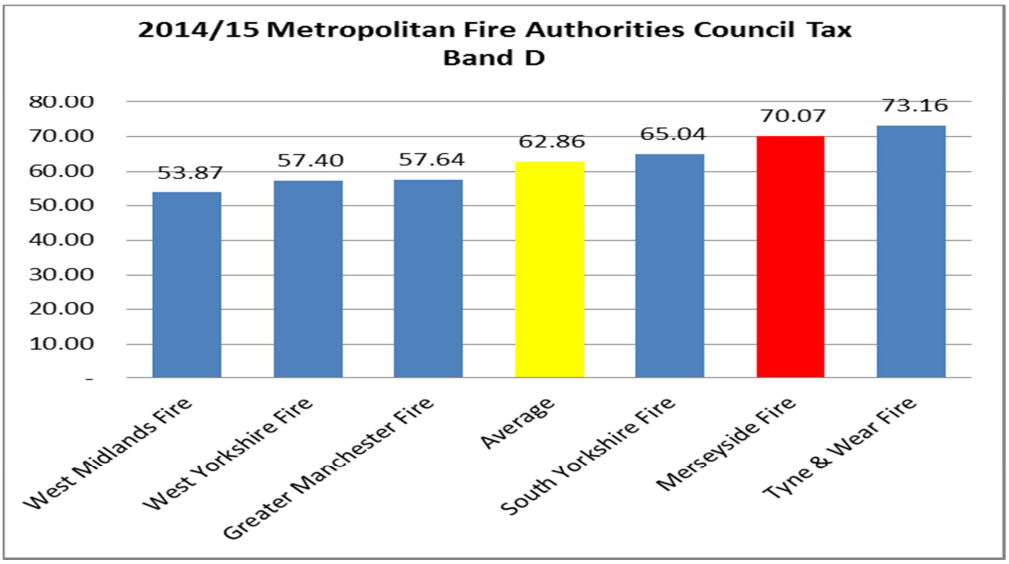
- Sought to control Council Tax increases,
- Planned for pay awards and cost increases in line with HM Treasury inflation forecasts,
- Recruited and trained employees to meet the Authority's high performance standards and budgeted for staff actually in post,
- Sought to generate significant savings through staff reductions whilst avoiding compulsory redundancy,
- Sought to minimise the impact of cuts on frontline services including prevention,
- Made significant investment in IT and computing (including outsourcing),
- Provided further investment in equality and health and safety,
- Attempted to plan prudently over the medium term by considering all significant risks to the assumptions in the financial plan and creating specific reserves if deemed necessary,
- Maintained a general reserve of at least £2m following assessments of risk,
- Because of pressures on revenue budget generally avoided funding capital expenditure from revenue through leasing or RCCO,
- Invested in the capital infrastructure of the Authority in line with the Asset Management Plan, vehicle replacement strategies and corporate objectives.

41. These strategies have over recent history allowed the Authority to reduce costs and maintain relatively low levels of Council Tax increase despite very tight grant settlements.

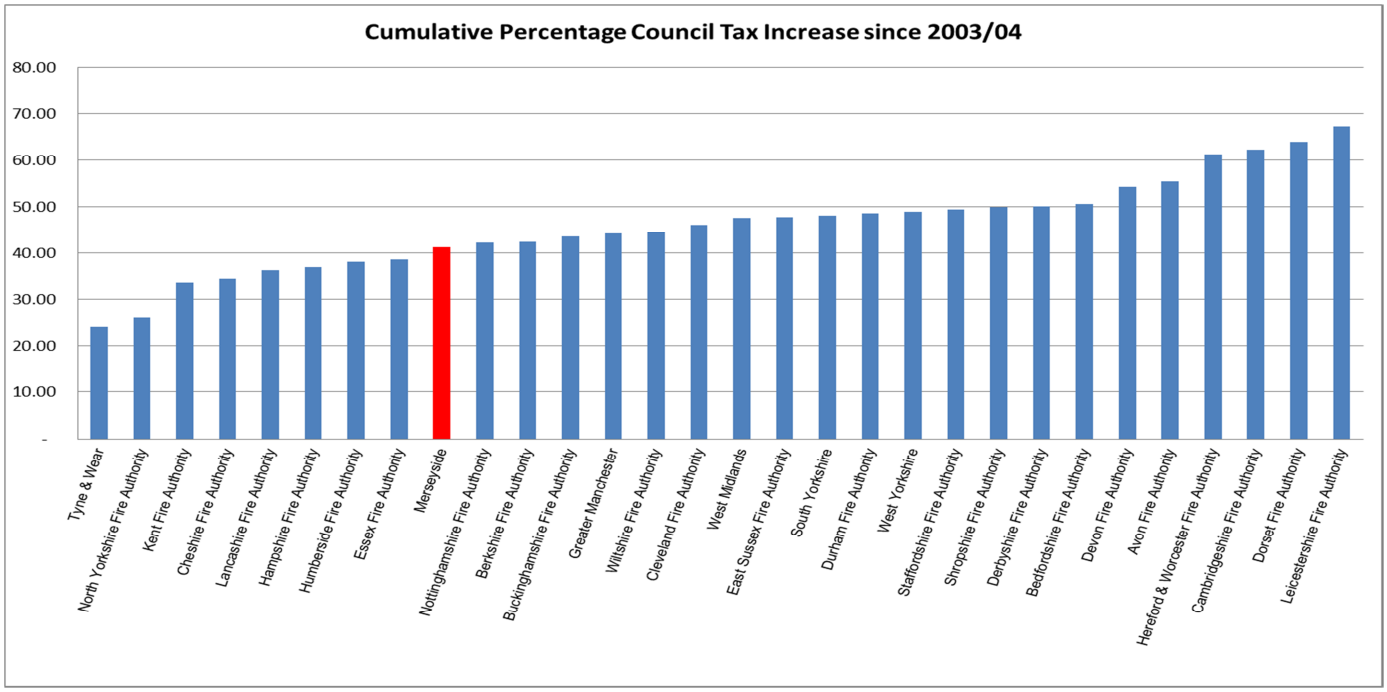
42. The Authority's 2014/15 (Band D) Council Tax is £70.07. This is slightly above the FRS national average (£68.96) as shown in the bar chart below:-



43. In 1996/97 Merseyside's Council Tax was more than 50% above the average of Metropolitan FRA's. Now it is only 11.5% above the average of that group:

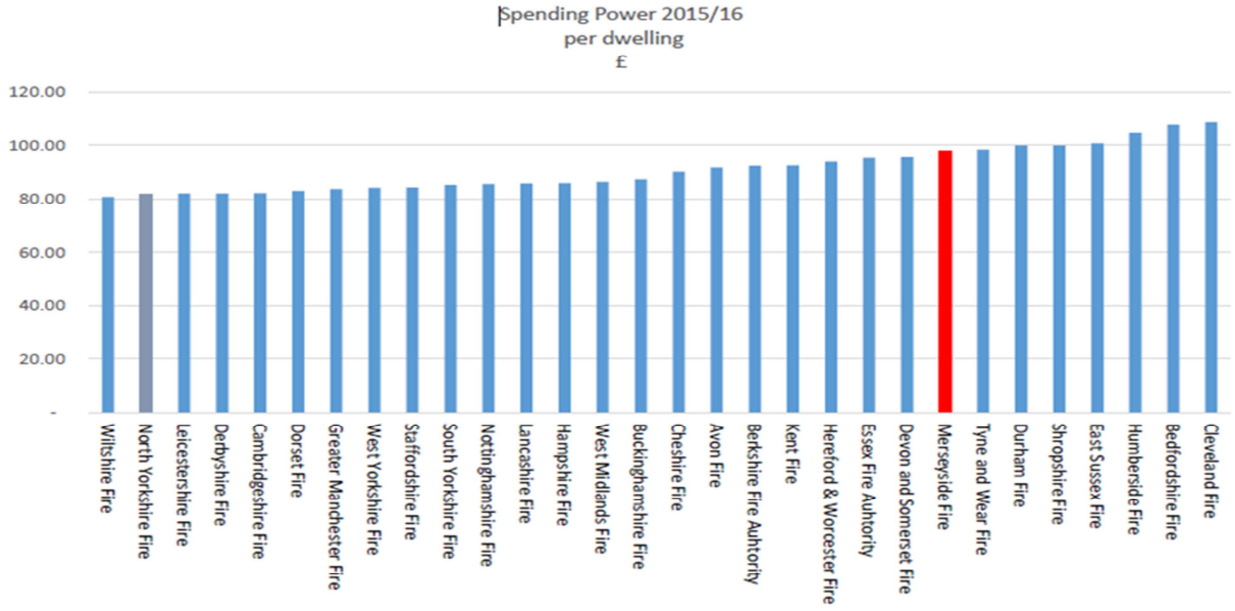


44. Over the past 10 years when compared to the other FRA's Merseyside has had one of the lowest cumulative council tax increases:



45. The Authority's control of council tax should be considered in light of the fact that across the same time period the council tax base of Merseyside has had one of the lowest increases. The tax base reflects how much income is generated by £1 of "Band D" equivalent council tax. So if the tax base increases, income will increase, even if the council tax charge remains unchanged.

46. However, despite recent improvements it should be noted that we remain, in comparison to our peers, a relatively high spending authority on a spending power per dwelling basis. *(Spending power is a Government measure of estimated overall budget which assumes all FRA's take the council tax freeze grant.)*



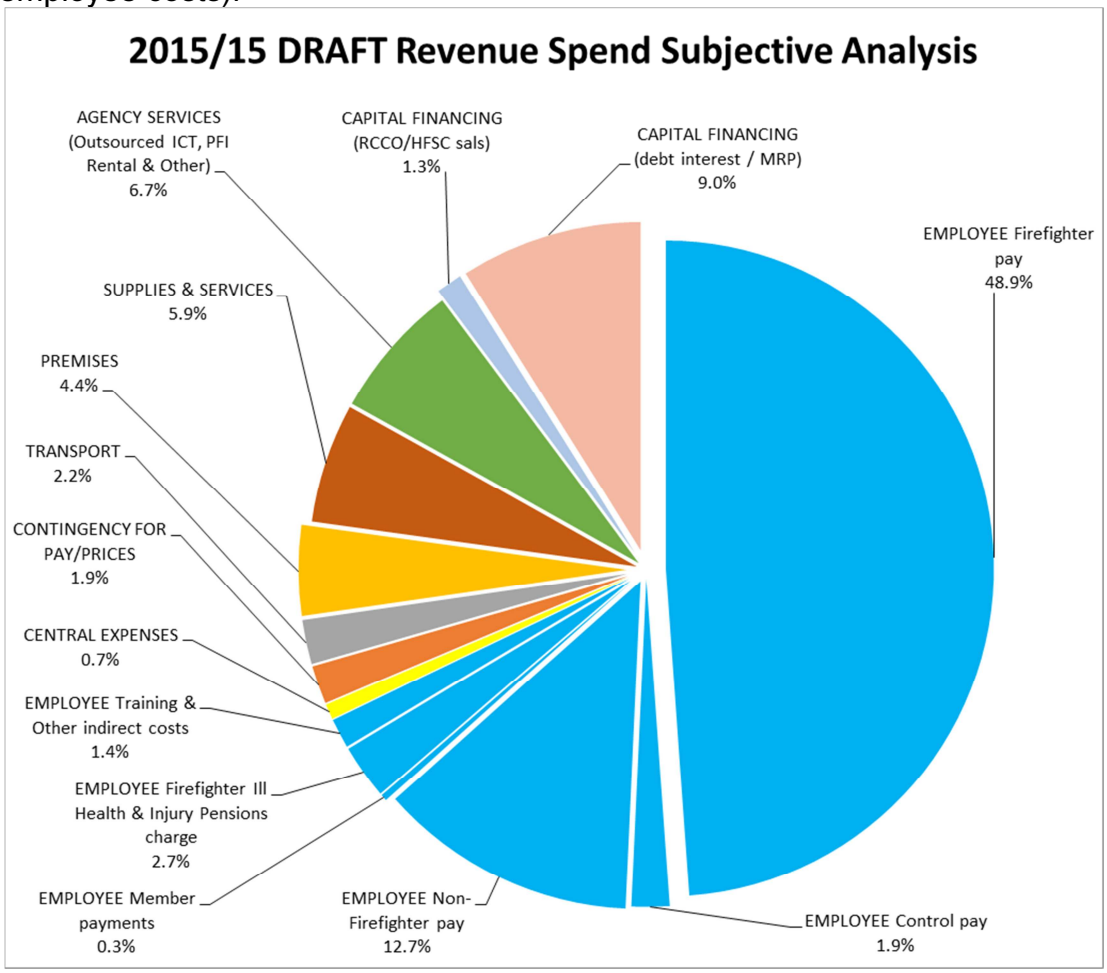
Overall Financial Health

47. The Authority has a proven track record for meeting significant financial challenges in the past. The Authority, as part of a risk based strategy, has built up reserves in recent years to provide a short term buffer whilst the Authority implements the structural changes to deliver the required savings on a permanent basis. The unprecedented reductions in Government funding will require difficult decisions but the Authority has a proven track record in managing its financial affairs well as can be seen in the following indicators:-

- Authority accounts 2013/14 audited without qualification once again.
- Annual Audit Letter highlighted general satisfaction with financial corporate governance and reporting arrangements.
- IRMP recognised as innovative.
- The Authority has maintained a general revenue reserve of at least £2.0m in recent years.
- Cost centre budgeting now well established along with a culture of financial management.
- Maintained a five year financial plan and capital programme and most importantly a consistent medium term strategy.
- Successfully delivered large-scale changes and savings

Current Allocation of Resources

48. Members will be aware that FRS expenditure is predominantly employee related (approximately 70%) as is shown in the pie chart below. (The blue sections relate to employee costs):-

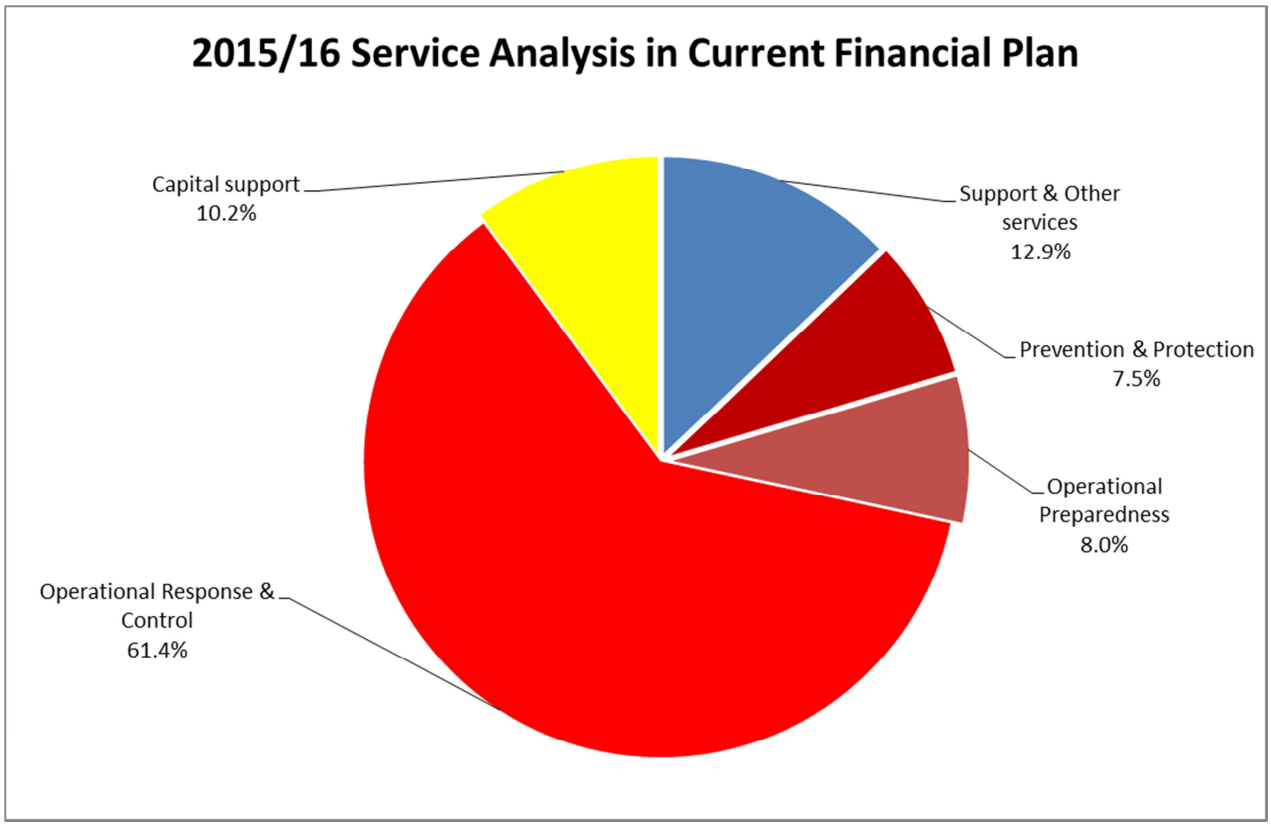


A full subjective analysis of the base budget for 2015/16 is set out in **Appendix A**

A subjective analysis is only part of the overall view on spending and in order to assist Members the same data is shown in a "thematic" view below and is based upon the service's strategic objectives:

Allocation of Resources in line with Corporate Objectives

49. The Authority has an excellent track record of investing in line with its corporate priorities. It can be seen from the pie chart below that most expenditure 61.4% goes on emergency and specialist response. In addition 8.0% goes on Operational Preparedness and 7.5% on Prevention & Protection, and therefore over 76.9% of expenditure is on the "front line" services. In addition the 10.2% on capital costs relates mostly to previous investment in front line assets, fire stations, vehicles and equipment. The remaining 12.9% is on support services.



Looking in more detail at each area the expenditure includes:-

Operational Response & Control (Total £38m)

- Service delivery and emergency response through its 26 fire stations.
- Specialist capabilities such as the Search and Rescue Team and Search Dogs.
- Invested in staff safety – procured state of the art fire kit, helmets, boots, Breathing Apparatus and appliances.
- Invests £1.5m operating a Training and Development Academy.
- Deliver HFSC programme.
- Investing in new community fire stations.
- Marine Rescue Unit to support the airport and safety on the River Mersey.

Prevention & Protection (Total £5m)

- District Prevention & Protection Teams; £2.5m
- Community Prevention work and youth engagement; £1.6m
- Purchase of £0.5m of smoke alarms per annum
- Fire Service Direct; £0.2m
- Employment of specialist Advocates and continuation of the Princes Trust and other programmes; £0.2m
- Invested in volunteers with the Fire Support Network; £0.2m
- Working with the private sector to deliver speedier restoration of property

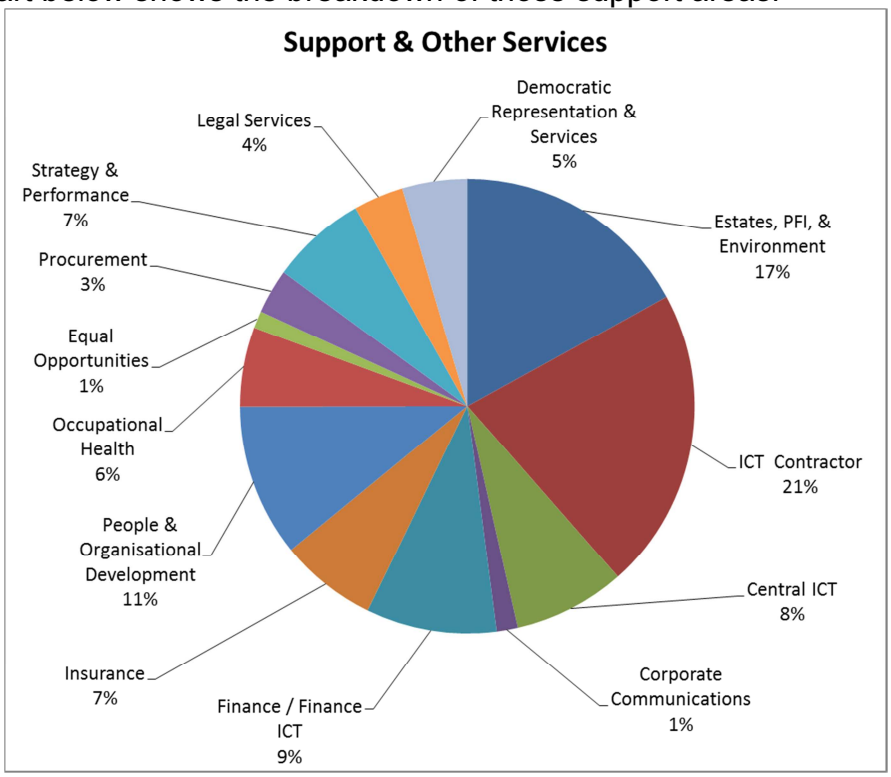
Operational Preparedness (Total £5m)

The investment of £5m delivers a variety of services which helps prepare for a full range of possible incidents in Merseyside and ensure Firefighter safety.

- Operational Planning and Policy
- Contingency Planning
- New Dimensions (National Resilience) to cope with major disasters and terrorist threats
- Operational Equipment Team
- Water Section
- Health and Safety Department
- Transport/Fleet Management – to keep vehicles operating effectively
- Workshops
- Standard Operating Procedure Review Team

Support Services & Other (Total £8m)

The investment in support services of £8m represents12.9% of the budget. The pie chart below shows the breakdown of those support areas:-



It should be noted that many of the services are key “front line” elements of a modern FRS. For example:-

- Estates – includes the running costs of buildings including 26 Community Fire Stations;
- ICT – includes the cost of the Mobilising Communications Centre;
- Occupational Health – to support staff and manage sickness

In addition some costs are unavoidable for any organisation;

- Insurance- to cover 3 party, vehicle and employer liabilities;
- Legal, Payroll, Accounting; Human Resources; Procurement etc. to support the organisation in paying its staff, suppliers, carrying out activities within the law and preparing statutory returns.

Also the cost of governance in relation to elected members is also contained within support and other costs.

C) CAPITAL PROGRAMME

50. Capital is considered first in this report so that Members can clearly consider the revenue impacts of capital investment and borrowing decisions as part of revenue budget and council tax considerations. ***The following sections (C) to (F) anticipate the Authority agreeing the proposed capital programme and its financing as set out*** .

Introduction

51. From 1st April 2004, the Local Government Act 2003 replaced the previous regime of capital controls with the Prudential System for Capital Finance. Local authorities are free to decide for themselves how much they can afford to borrow for capital purposes, subject to various safeguards. The Government has reserve powers to limit an authority's borrowing if the Government believes it to be unaffordable, or in times of public spending restraint.

Prudential Code

52. A key part of the revised capital system is the CIPFA "Prudential Code for Local Authority Capital Finance" which provides a framework of decision-making under which authorities will decide their capital investment and financing plans and set limits for borrowing.

53. Authorities will be required to 'have regard to' the "Prudential Code" when setting their future budgets and Council Tax levels - which in practice means that they would need to have very good reasons not to comply.

54. The over-riding objective of the "Prudential Code" is to ensure that the capital investment plans of local authorities are affordable, prudent, sustainable, and follow good practice.

55. Some of the main features of the "Prudential Code" are as follows:
    - The full Authority must consider and set a number of indicators and limits for its capital plans as part of the annual budget setting process. The limits can be revised during the year but only by the full Authority. The mandatory indicators are shown in Section E.
    - The indicators and limits must be monitored during the year and outturn figures reported.
    - The Authority must produce and maintain capital and revenue plans for at least three future years including three year estimates of its future Council Tax taking account of the proposed capital programme and other plans.
    - The Authority must set an authorised limit for its total debt (including borrowing and long term liabilities) which may not be exceeded.
    - Limits relating to treasury management matters must be considered as part of the Annual Treasury Management Strategy Report.

56. Fundamentally, the objective of the Code is that the total of an authority's capital investment remains within sustainable limits, following consideration of the impact on the "bottom line" Council Tax. This is ultimately determined by a judgement about what Members consider is an acceptable level of Council Tax.

Capital Investment Strategy

57. Each financial year the Authority produces a capital programme to manage major capital schemes. Owing to the nature of capital expenditure a large number of schemes span more than one financial year so the programme is a rolling programme covering five future financial years.

58. The starting point for this programme has been an assessment of the capital investment requirements for the Authority for future years based upon needs identified by the various expert professionals in areas like buildings, vehicles, ICT, and operational equipment. Initial bids were requested and through an iterative process Officers have modified the programme in the light of:-

- service requirements, and in particular investments required to support and deliver the IRMP.
- the need to adopt a prudential approach to capital borrowing under the new regime, being mindful of affordability, prudence and sustainability and in particular the impact on Council Tax levels.

59. This has produced a five-year future capital programme proposal of £27.268m which is set out in the summary table below. This table also identifies funding of the programme and a resultant borrowing requirement of £21.443m. The full programme is set out in **Appendix B** (Appendix B (1) is the updated programme and Appendix B (2) the new additions to previously agreed programmes).

Proposed Authority Capital Programme for 2015/2016 - 2019/2020

Capital Expenditure	Total Cost £	2015/16 £	2016/17 £	2017/18 £	2018/19 £	2019/20 £
Building/Land - current	**10,946,500**	9,366,000	455,500	352,000	396,500	376,500
Fire Safety - current	**3,877,000**	777,000	775,000	775,000	775,000	775,000
ICT - current	**3,071,000**	737,000	531,000	556,000	816,000	431,000
Operational Equipment & Hydrants - current	**1,837,000**	225,000	168,000	525,000	484,000	435,000
Vehicles - current	**7,536,100**	2,675,100	1,526,000	1,228,000	858,000	1,249,000
Ependiture	**27,267,600**	**13,780,100**	**3,455,500**	**3,436,000**	**3,329,500**	**3,266,500**
Financing Available	**Total £**	**2015/16 £**	**2016/17 £**	**2017/18 £**	**2018/19 £**	**2018/19 £**
Capital Receipts						
Sale of 2 existing N-le-W LLAR properties		275,000				
Sale of Huyton FS (CFO/095/14)			250,000			
Sale of Whiston FS (CFO/095/14)			250,000			
	775,000	275,000	500,000	0	0	0
Revenue Contribution to Capital Outlay (RCCO)						
CFS alarm installation (salaries)		450,000	450,000	450,000	450,000	450,000
CFS alarm installation (Income from FSD)		50,000	50,000	50,000	50,000	0
	2,450,000	500,000	500,000	500,000	500,000	450,000
Capital Reserve						
Prescot FS New Build (CFO/095/14)		830,000				
	830,000	830,000	0	0	0	0
Grants						
Prescot FS New Build (CFO/095/14)		1,770,000				
	1,770,000	1,770,000	0	0	0	0
Total Non Borrowing	**5,825,000**	**3,375,000**	**1,000,000**	**500,000**	**500,000**	**450,000**
Unsupported Borrowing	**21,442,600**	**10,405,100**	**2,455,500**	**2,936,000**	**2,829,500**	**2,816,500**
Total Funding	**27,267,600**	**13,780,100**	**3,455,500**	**3,436,000**	**3,329,500**	**3,266,500**

60. New additions to the capital programme have increased the overall expenditure by £2.397m, (Appendix B(2)), the reasons for this are :-

(a) The addition of the "extra year" to the programme 2019/20, £3.267m
(b) A re-assessment of spending on smoke alarm costs. The current fire safety capital programme is based on the delivery of approximately 100,000 HFSCs and the installation of 70,000 free smoke alarms a year. In recent years the spending on smoke alarms and installation has reduced as a consequence of the Authority policy of offering free smoke alarms to only those households most at risk and those not previously visited. Smoke alarm spending and installation costs are expected to be £0.224m and £0.280m a year lower than previously planned respectively. This a total reduction of £2.016m across the whole programme
(c) New Expenditure Proposals have been included which total across the whole life of the programme £1.146m. The key items are for ICT server and security upgrades (£0.355m) and operational equipment purchases for older equipment (£0.791m)

61. **Appendix B(1)** provides a full analysis of the current 5 year capital programme and additional information can also be found in financial review report (CFO/005/15). Full details of the additional **new starts** can be found in **Appendix B(2**) attached to this report.. The main areas of capital programme expenditure are summarised below

A. Building Investment Strategy (£10.947m)
The estate comprises of 26 fire stations, a Training and Development Academy (TDA), Service Headquarters including Fire and Rescue Control, Marine Rescue Team, and the Engineering Centre. The capital programme reflects the funding required to replace, maintain and enhance the current estate stock, and when possible seeks to attract external funding (PFI) or specific contributions (capital receipts, capital reserves) to reduce the level of borrowing requirement. Estates maintain and revise a 5 year property asset management plan and the proposed capital programme is consistent with the priority areas that are contained within the plan.

Investment is proposed in line with the current Asset Management Plan. Nearly all the planned work is around the refurbishment and essential work at fire stations, £10.1m. At present only those fire station mergers approved following public consultation are included in the capital programme, (currently just the Prescot proposal).

The balance of the programme reflects general maintenance work across all property for items such as energy conservation measures, heating & ventilation, fitness equipment etc.

B. Fire Safety (£3.877m)
Smoke alarms and sprinkler systems are being classed as capital expenditure in line with Government guidance. This follows the awarding of historic capital grants by the (then) ODPM towards the purchase cost of such

items in financial years 2004/05 through to 2007/08. Current policy is to capitalise the installation costs of smoke alarms estimated at £2.250m over the period, however this expenditure is not funded through borrowing but financed in the year by a revenue contribution to capital.

C. ICT – Investing in line with the ICT Strategy (£3.071m)
In line with the increasing use of technology to improve the service there is a significant investment in ICT within the programme. The most significant investments are in line with a planned replacement policy of 5 years for PCs, Servers and Network £1.9m, and software licenses £0.9m.

The other main investment is in the continued development of the portal £0.050m.

D. Operational Equipment & Hydrants (£1.837m)
Provision is also made to ensure that a modern fire and rescue service can be delivered and firefighters kept safe, in particular provision is made for investment in specialist rescue equipment and new breathing apparatus such as :-

- Hydraulic rescue equipment, £0.4m
- BA equipment and communication equipment, £0.1m
- Thermal imaging cameras, £0.2m
- Gas Tight Suits & PPE, £0.2m
- Other specialist equipment, £0.7m
- Installation of new or replacement hydrants in line with our water strategy, £0.2m.

E. Vehicle Replacement Strategy (£7.536m)
The Fleet Manager has identified needs as follows:-

a. Fire Appliances;
The Authority has developed an appliance replacement strategy based on the economic life of an appliance. Each appliance has an estimated service life of 10 years on the front line followed by 2 years as a reserve appliance. The plan provides for 18 new appliances.

b. Specialist Vehicles;
There is a need to make provision for the purchase of specialist vehicles to support the IRMP and to support the wider range of roles for the fire and rescue service including:

- Combined Platform Ladder appliances (2 refurbished and 1 new vehicle)
- IMU - Prime Movers (4)
- Special Vehicles (Water Rescue, BA Support unit)

c. Ancillary Vehicles;
Provision is included for the phased renewal of the ancillary vehicle fleet.

Officers have commenced a review of the specialist vehicle and ancillary fleet and this will not be completed until after the budget. Any amendments

to the proposed capital programme will be brought back to members for approval during 2015/16.

Funding the Programme

62. Capital receipts:- capital receipts are usually the proceeds from the sale of assets. Any such receipts can be applied either to reduce an Authority's outstanding debt or to be reinvested in the capital infrastructure.

63. The Authority has (when available) used capital receipts as a source of funding for new capital investment with little, if any, being used for debt repayment – unless regulations require a proportion of the receipts to be used specifically to repay debt. However, under the new regime the Authority needs to consider if a proportion of any future receipts should be used for debt repayment as part of its overall strategy.

64. The proposed capital programme anticipates capital receipts from a number of site disposals totalling £0.775m.

65. It assumes that this income will be used to reinvest in the capital infrastructure and support the capital programme. Members should note that the anticipated capital receipt values are based on the best estimates at a point in time.

66. Capital Grants:- As part of the 2010 spending review the Government also made the decision that there will be no supported borrowing allocations for the Fire and Rescue Service in the spending review period. Government capital support will be given in the form of a capital grant only. The Government had previously announced that the Authority will receive specific capital grant of £1.770m for a new joint blue light station at Prescot in line with its bid. In addition the Authority was recently successful in its bid for transformation grant funding for a programme of station mergers and blue light collaboration schemes and received £4.47m. At present only the station mergers approved following public consultation are included in the capital programme. The recent £4.47m grant and estimated scheme costs have not been included in the capital programme at this point.

67. Operating Leasing:- Under the previous system of capital controls, investment that was funded by operating leases did not count as either capital expenditure or financing as a credit arrangement. Therefore, in common with most other local authorities, operating leasing has been a source of funding for some limited eligible assets (e.g. vehicles, plant and machinery, and computer equipment) although the Authority generally avoided this because of the impact on the revenue account. However, whilst operating leasing as a source of funding remains outside of the Prudential Capital System, no leasing is assumed in this programme. The Deputy Chief Executive will monitor the suitability of alternative methods of finance.

68. Borrowing:- Under the Prudential capital system Local Authorities are now able to determine their level of borrowing. However, the Government has retained reserve powers to limit an Authority's borrowing if the Government believes an Authority's proposals to be "unaffordable" or in times of national public spending constraint.

69. In the past Government provided support for the Authority's capital spending through supported capital expenditure. The revenue costs associated with

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

70. The proposed capital programme represents an overall expenditure increase of £2.397m reflecting the proposed net "new starts" expenditure. Of this £3.267m relates to the addition of an extra year (2019/20) and there are other adjustments of (£0.870m). Appendix B(2) sets out these changes in more detail.

71. The impact of these net additions to the expenditure programme on the Authority's borrowing requirement is a net increase of £3.067m:

	£m
Increase in expenditure	2.4
Change in Non Borrowing Funding Sources:	
RCCO (HFSC installation costs)	0.7
Required Increase in Borrowing	3.1

The level of prudential "unsupported" borrowing therefore will increase by £3.067m to £21.443m.

Impacts on Revenue Budget and Financial Plan

72. When the Authority borrows money it has to factor the debt repayment and interest costs into its financial plans. The minimum revenue provision (MRP) methodology calculates how much debt repayment is required each year. Following the new Capital Regulations announced in 2008 the Authority must approve an MRP Statement each year that sets out the policy on MRP. Section D of this report outlines for Members the proposed MRP policy for 2015/16 – 2019/20 and the methodology for calculating the MRP. The additional borrowing and proposed MRP policy require an increase to the 2014/15 base figure for MRP and Interest of:-

	Estimate 2015/16	Estimate 2016/17	Estimate 2017/18	Estimate 2018/19	Estimate 2019/20
	£'m	£'m	£'m	£'m	£'m
Cumulative increase in MRP / Interest	0.256	0.516	0.966	1.216	1.466

73. A significant factor in the large increase in the budget requirement is down to the Government's decision to factor in no new supported borrowing since 2010/11 and the capital regulations requiring all non-supported borrowing to be repaid over the relevant asset life. This has meant a four or five fold increase in MRP calculations for assets with a short asset life that previously had MRP calculated over a twenty-five year period.

74. Anticipated increase in MRP and Interest has been built into the financial plan for 2015/16 – 2019/20. To give Members an indication of the impact of the proposals,

for each £1m reduction in borrowing it would reduce the associated revenue cost by potentially £0.050m - £0.100m (dependant upon on the relevant asset life), the council tax equivalent reduction would be 0.2% - 0.5% or £0.14 to £0.28.

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

(D) MINIMUM REVENUE PROVISION STATEMENT

75. Under the Local Authorities and Accounting Regulations the Authority is required to set aside a sum of money each year to reduce the overall level of debt, this sum is known as the Minimum Revenue Provision (MRP). The 2003 regulations set a minimum annual amount to be charged to revenue based on the Authority's Capital Financing Requirement (CFR) which is an amount broadly equivalent to the Authority's outstanding debt. The regulations have been updated in 2008 and now require each Authority to repay debt at a rate it considers **prudent** and to set out in an annual statement the Authority's policy on making MRP in respect of the forthcoming year.

76. The new regulations guidance interprets MRP may be deemed to be prudent if it is either:
    - Based over a period that is reasonably commensurate with that over which the capital expenditure / asset provides benefits (asset life), or
    - For the element of expenditure met from borrowing supported by Government Grant a period reasonably commensurate with the period in the determination of that grant (this in reality would equate to the current 4% MRP methodology).

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

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

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

    3. **Asset Life Method** – MRP is determined by reference to the life of the asset and the amount is either based on;
        - equal instalments method. This generates a series of equal annual amounts over the life of each asset that is financed from borrowing; or
        - annuity method. This method links the MRP to the flow of benefits from an asset where the benefit is expected to increase in later years.

    4. **Depreciation Method** - MRP is to be equal to the provision required in accordance with depreciation accounting in respect of the asset on which expenditure has been financed by borrowing. This option is available to both supported and unsupported borrowing in determining the MRP requirement

Finance Leases and PFI

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

2015/16 MRP:

79. The 2015/16 MRP is determined by the actual level of outstanding debt (CFR) as at the end of 2014/15. It is recommend that the Authority adopt a similar strategy for MRP determination as that in 2014/15;

- For all capital expenditure incurred before 1st April 2008 and for all capital expenditure funded via **supported borrowing**; MRP to be calculated using the Regulatory Method.
- For all capital expenditure incurred after 1st April 2008 financed by **unsupported (prudential) borrowing**; MRP to be calculated using the Asset Life Method – equal instalments method.
- For credit arrangements such as **on balance sheet leasing arrangements (finance leases)**; the MRP charge is to be equal to the principal element of the annual rental.
- For **on balance sheet PFI contracts**; the MRP charge will be equal to the principal element of the annual rental.

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

81. By adopting the recommendations above, the MRP charge for 2015/16 would be £3.7m, consisting of £1.7m for prudential borrowing schemes incurred after 1st April 2008 and £2.0m for all other capital schemes (these figures exclude PFI and Finance lease as the MRP charge is a notional figure and contained within the rental budget).

82. Interest on loans taken out to fund capital expenditure is estimated at £2.5m.

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

84. The Authority in the past has determined it can afford and sustain significant prudential borrowing in order to allow the required level of investment in the infrastructure and assets of the Authority to deliver a modern well equipped fire and rescue service.

(E) PRUDENTIAL INDICATOR REPORT

85. Having formulated a draft Capital Programme, the Authority, in making final decisions upon that Capital Programme and Revenue Budget 2015/16, will need to consider a report setting out a range of Prudential Indicators aimed at demonstrating the intended Investment Programme's affordability, prudence and impact upon Treasury Management activity and strategy.

86. It should be noted, however, that in order to provide those Indicators, Capital and Revenue financial plans need to be prepared for each of the next 3 financial years, commencing with 2015/16.

87. The financial plans prepared in respect of the financial years 2016/17 and 2017/18 are not to be mistaken for approved Budgets. They are, at this stage, only a guide for financial planning and as such subject to significant change as a result of decisions made by the Authority. However, such plans are required to be supported by an indication of future Council Tax. At this stage an assumption of Council Tax increases of 2% in 2015/16 and future years.

Prudential Indicators

88. The Authority must demonstrate that its spending plans comply with the Prudential Code by the publication of a number of performance indicators, which are known as the Prudential Indicators. ***Details of the prudential indicators for this Authority are provided below.***

89. The purpose of the indicators is to demonstrate that capital investment remains within sustainable limits and that the Authority has considered the impact of the whole plan on future levels of Council Tax. The indicators that will measure this are:-

- Estimates of the ratio of capital financing charges to the net revenue budget
- Estimates of the precept that would result from the three-year capital plan.
- Estimates of the capital financing requirement.

90. The prudential indicators for Merseyside are:-

a) Capital Expenditure

The actual capital expenditure that was incurred in 2013/14 and the estimates of capital expenditure to be incurred for the current and future years that are recommended for approval are:

	Actual 2013/14	Estimate 2014/15	Estimate 2015/16	Estimate 2016/17	Estimate 2017/18	Estimate 2018/19	Estimate 2019/20
	£000's	£000's	£000's	£000's	£000's	£000's	£000's
Capital Expenditure	9,375	11,660	13,780	3,456	3,436	3,329	3,267

Members will note that the increased expenditure in 2013/14 and 2015/16 reflects a number of significant investments including;

- the Joint Control Room (£10.4m) of which £5.3m was funded by a contribution from Merseyside Police and £1.1m from CLG Grant;

- A new secondary control room and associated ICT improvements relating to the JCC move (£2.0) of which £0.7m was funded by a CLG Grant;

- The planned new station in Prescot.

This explains why the total expenditure in these years appear to be relatively high. In addition it is important to remember capital costs are shown as the gross figure and are not shown net of any grants or contributions received to contribute towards the cost. More details on the capital programme are given elsewhere in the report (Section C).

(b) Ratio of financing costs to net revenue stream
Estimates of the ratio of financing costs to net revenue stream (amounts met from government grants and local taxpayers) for the current and future years, and the actual figures for 2013/14 are:

	Actual 2013/14	Estimate 2014/15	Estimate 2015/16	Estimate 2016/17	Estimate 2017/18	Estimate 2018/19	Estimate 2019/20
Ratio of Financing costs to Net Revenue Stream	**7.94%**	**8.18%**	**9.19%**	**11.04%**	**12.09%**	**13.30%**	**14.01%**

This shows that forecast debt financing costs will increase from 7.94% in 2013/14 (based on the actual forecast capital spend in 2014/15) to 14.01% by 2019/20. As stated previously the impact of the Government's decision to issue no new supported borrowing for CSR10 has meant all MRP calculations are now based on asset life. This has resulted in a significant rise in MRP over the medium term, but eventually the ratio will fall as historic debt is repaid and all other debt is paid off over the life of the asset. This is also affected by the fact that whilst the Authority's debt is increasing its overall budget is reducing because of forecast Government funding cuts.

(c) Effect on the Precept
The estimate of the incremental impact of capital investment decisions proposed in this budget report, over and above capital investment decisions that have been previously been taken by the Authority are:

	Estimate 2015/16	Estimate 2016/17	Estimate 2017/18	Estimate 2018/19	Estimate 2019/20
Incremental Impact of Capital Investment Decisions	£2.95	-£0.24	-£0.01	£0.06	£1.13

This indicator compares the capital programme set by the Authority in last year's budget process to the proposed revised capital programme submitted this year. It is intended to show the marginal impact of the overall capital programme, and the decisions being made by the Authority, on the Council Tax levels. The re-phasing of expenditure from 2014/15 into 2015/16 approved during the year, £6m, and the reduction in smoke alarm spend in future years explains the movement in the

figures over this period. The new start programme in 2019/20 has resulted in the increase in 2019/20.

Capital Financing Requirement

91. The Capital Financing Requirement (CFR) measures the Authority's underlying need to borrow for capital investment purposes.

92. Based on current commitments for 2014/15 and the latest estimates of capital investment decisions in future years, the capital financing requirement at 31st March is as follows:

	Estimate 31.3.14	Estimate 31.3.15	Estimate 31.3.16	Estimate 31.3.17	Estimate 31.3.18	Estimate 31.3.19	Estimate 31.3.20
	£000,s	£000,s	£000,s	£000,s	£000,s	£000,s	£000,s
Capital Financing Requirement (Excluding PFI)	51,587	52,657	59,392	57,455	55,830	53,772	51,569

In accordance with best practice, the Authority does not associate borrowing with particular items or types of expenditure. The Authority has, at any point in time, a number of cash flows both positive and negative, and manages its Treasury position in terms of its borrowings and investments in accordance with its approved Treasury Management Strategy and practices. In day to day cash management, no distinction can be made between revenue cash and capital cash. External borrowing arises as a consequence of all the financial transactions of the Authority and not simply those arising from capital spending. In contrast, the capital financing requirement, CFR, reflects the Authority's underlying need to borrow for a capital investment purposes.

Net Borrowing and the Capital Financing Requirement

93. CIPFA's *Prudential Code for Capital Finance in Local Authorities* includes the following as a key indicator of prudence:

"In order to ensure that over the medium term net borrowing will only be for a capital purpose, the local authority should ensure that net external borrowing does not, except in the short term, exceed the total capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years."

94. The Authority had no difficulty in meeting this requirement as the Authority's CFR (excluding PFI) is expected to reach £55.830m by the end of 2017/18 and the expected maximum debt position, (the "operational boundary" – see Treasury Management Strategy) for 2017/18 is £42.000m. The reason for the borrowing figure being lower than the CFR figure reflects the availability of cash in the form of reserves to the Authority and therefore the ability to defer having to take out new loans for the short to medium term.

(F) TREASURY MANAGEMENT STRATEGY STATEMENT 2014/15

INTRODUCTION

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

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

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

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

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

PROPOSED STRATEGY

96. The above policies and parameters provide an approved framework within which the Officers undertake the day to day capital and treasury activities. The Authority is recommended to approve each of the key elements contained within this report which are :-

    - The Treasury Management Strategy 2015/16.
    - The External Debt and Treasury Management Prudential Indicators and Limits for 2015/16 to 2017/18.
    - The Investment Strategy 2015/16.
    - The Minimum Revenue Provision (MRP) Statement included in section D which sets out the Authority's policy on MRP.

TREASURY MANAGEMENT STRATEGY

97. The suggested strategy for 2015/16 in respect of Treasury Management is based upon treasury officers' views on interest rates supplemented by leading market forecasts. The strategy covers:-

    (a) prospects for interest rates;
    (b) capital borrowing and debt rescheduling;

(c) annual investment strategy;
(d) external debt prudential indicators;
(e) treasury management prudential indicators;
(f) performance indicators;
(g) treasury management advisers.

Each of the above is now considered in more detail below:

(a) PROSPECTS FOR INTEREST RATES:

There are signs that the economic recovery has stabilised and growth forecasts have recently been more subdued. Growth of the economy will still remain strong but not as strong as previously expected. Also encouraging has been the sharp fall in inflation, reaching 1.0% in November 2014, the lowest rate since September 2002. Forward indications for the next year are that inflation is likely to remain around or under 1%. The Monetary Policy Committee will be focusing in 2015/16 on the 2% inflation target and it is unlikely that they will vote to increase base rates before late 2015 or early 2016.

Longer term fixed interest borrowing rates are based on central government borrowing costs i.e. UK gilt yields. Gilt yields have continued to fall despite the high volume of gilt issuance in the UK and of bond issuance in other major western countries. This has been due to rapidly falling inflation and the continued demand for safe haven instruments correlated to geo-political risks. Public Works Loan Board (PWLB) rates have consequently fallen to abnormally low levels. It is difficult to predict how long current levels are sustainable made even harder by the political risks around the UK general election in May 2015. However, the economic fundamentals of continued growth, falling unemployment and eventually rising inflation would indicate upward pressure on long term rates and longer-term Public Works Loans Board (PWLB) rates could rise by around 0.5% in 2015/16.

The overall structure of interest rates is expected to remain the same and short term rates will continue to be lower than long term rates and are likely to remain so throughout 2015/16. In this scenario, the strategy will be to reduce investments and borrow for short periods and possibly at variable rates when required.

(b) CAPITAL BORROWING AND DEBT RESCHEDULING:

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 2015/16. Given the likely structure of interest rates described above, it is envisaged that any borrowing to meet short term cash flow shortages will be for very short periods. Against this background, Treasury Officers will monitor the interest rate market and adopt a pragmatic approach to any changing circumstances.

Rescheduling of debt is the early repayment of loans and replacement by loans for different periods and at different interest rates. It can be used to enhance the balance of the long term portfolio, by for example, amending the maturity profile

or changing volatility levels and may on occasion generate cash savings. Debt rescheduling becomes more beneficial when the relationship between short and long term rates moves appreciably.

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

(c) ANNUAL INVESTMENT STRATEGY

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

The Authority's investment priorities are (a) the security of capital and (b) liquidity of its investments. The Authority will aim to achieve the optimum return on its investments commensurate with the proper levels of security and liquidity. All investments will be in sterling. All cash balances will be invested in accordance with the Code of Practice and with regard to the statutory guidance.

A counterparty list of institutions with which the Authority will invest shall be maintained by reference to the criteria set out below for the different categories of institution and their credit rating. Regardless of these criteria, the money market will be closely monitored and any institution will be suspended from the counterparty lending list should any doubts arise concerning its financial standing. Under the guidance, investments fall into two separate categories, either specified or non-specified investments.

Specified Investments: Specified investments offer high security and high liquidity and satisfy the conditions set out below:

- The investment is denominated in sterling and any payments or repayments in respect of the investment are payable in sterling only.
- The investment is not a long-term investment (has a maturity of less than one year).
- The investment does not involve the acquisition of share capital in any corporate body.
- The investment is made with a body or in an investment scheme which has been awarded a high credit rating by a credit rating agency, or with the UK Government or a local authority.

Specified investments will comprise the following institutions: -

- The UK Government (such as the Debt Management Account deposit facility, UK Treasury Bills or a Gilt with less than one year to maturity).
- Supranational bonds of less than one year's duration.

- UK Local Authorities.
- Money Market Funds.
- Enhanced Money Market (Cash) Funds.
- UK Banks.
- Foreign banks registered in the UK.
- Building Societies.

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

- Long term credit rating A-

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

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

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

Investment Limits:- The credit ratings and individual limits for each institution within the categories of investments to be used by the Authority in 2015/16 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

No limits on investments with the UK Government and Local Authorities have been set because they are considered to be of the highest credit quality and are essentially risk free. The limits placed on other categories reflect some uncertainty and marginally higher risk profile of the institutions within those categories. The status of Royal Bank of Scotland as a part nationalized bank is unlikely to change for many years but Lloyds Bank is likely to be re-privatised in the near future so will revert to the lower limit of £2m alongside other UK banks. Money Market Funds although AAA rated, invest in a diverse portfolio so are not completely risk free and have been assigned a lower limit. There is a slightly higher risk for A- rated banks as described in para 30 below and so these institutions have the lowest limit.

Ways to increase investment returns have been considered including (a) reducing the minimum credit rating criteria from A- to BBB; (b) increasing the limits with individual institutions and (c) investing for periods longer than one year. Any of these ways would involve taking on additional risk because higher investment returns can only be achieved by taking higher risks. The decision not to do this but to continue with current policies was taken in the light of the Banking Reform Act which enables the government to force investors to take losses if a bank became insolvent. It is now unlikely that the government would fully fund a taxpayer bail out of a failed bank.

The maximum that may be invested with different banks that are part of the same conglomerate shall not exceed the maximum of the highest rated bank within the group. The limits may be exceeded for short periods when there are adverse conditions in the money market with the agreement of the Head of Finance or Treasury Manager.

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

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

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

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

Risk Management of Investment Counterparties:- Bank and Money Market Fund ratings are checked daily. The Authority is alerted by e-mail when there is an amendment by any of the agencies to the credit rating of an institution. If an amendment means an institution no longer meets the Authority's minimum requirement, or any doubt over its financial standing exists, then that institution is removed immediately from the counterparty lending list. Conversely, an institution may be added to the list should it achieve the minimum rating.

Credit ratings are only the starting point when considering credit risk. The Code of Practice requires the Authority to supplement credit rating information with additional operational market information which will be applied before making any specific investment decision from the agreed pool of counterparties. Credit Default Swaps and negative rating watches/outlooks are examined and the financial press, internet and financial information systems are monitored for

market information regarding its counterparties. It also receives daily e-mails from various market participants that could identify potential problems. Any information that casts doubt on an institution's creditworthiness is acted on by suspending investment with that institution.

Liquidity of Investments:- Each investment decision is made with regard to cash flow requirements resulting in a range of maturity periods within the investment portfolio. Investments are normally short term having a maturity of less than one year. The Prudential Code does allow longer term investments and under certain money market conditions it may be prudent to invest for up to three years dependent on cash flow forecasts.

Risk Benchmarking:- The CIPFA Codes and the DCLG Investment Guidance recommend the consideration and approval of security and liquidity benchmarks. Yield benchmarks are currently widely used to assess investment performance. Security and liquidity benchmarks are new requirements although the application of these is more subjective in nature. The benchmarks are simple guides to maximum risk and so may be breached from time to time depending on movements in interest rates and counterparty criteria. The purpose of them is for officers to monitor the current and trend position and amend the operational strategy to manage risk as conditions change. Any breach of the benchmarks will be reported, with supporting reasons in the Mid-Year or Annual Report.

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

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

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

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

(d) EXTERNAL DEBT PRUDENTIAL INDICATORS:

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

b. Authorised limit for external debt
c. Operational boundary for external debt

Authorised Limit: The Authorised Limit for Debt represents the maximum level of debt which the Authority may have during the year. The Authority has no powers to exceed this unless a further report with revised prudential indicators is approved by the Authority. The limit therefore makes appropriate allowance for the risks and uncertainties which affect day-to-day debt levels, and the ups and downs of short term cash flow.

The authorised limits reflect the Authority's Capital Financing Requirement, identified in its capital expenditure and financing plans. They are consistent with the treasury management policy statement and practices. The limit will ensure that total gross debt does not exceed the total of the CFR in the preceding, current or following two financial years. The Authority is asked to approve the limits below and to delegate authority to the Deputy Chief Executive, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities.

Authorised Limit for External Debt		**2015/16**	**2016/17**	**2017/18**
		£'000	**£'000**	**£'000**
Borrowing		63,000	62,000	60,000
Other Long Term Liabilities		2,000	2,000	2,000
TOTAL		**65,000**	**64,000**	**62,000**

Operational Boundary: The Operational Boundary indicator represents the expected maximum debt position during each year. It takes into account projections of borrowing requirement and repayments in future years. It may be different from the year end position as it reflects cash flows within each year. The Authority is asked to approve the limits and to delegate authority to the Deputy Chief Executive, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities.

Operational Boundary for External Debt		**2015/16**	**2016/17**	**2017/18**
		£'000	**£'000**	**£'000**
Borrowing		43,000	42,000	40,000
Other Long Term Liabilities		2,000	2,000	2,000
TOTAL		**45,000**	**44,000**	**42,000**

Actual External Debt: The prudential indicator for actual external debt considers a single point in time and hence is only directly comparable to the

authorised limit and operational boundary at that point in time. Actual external debt is monitored during the year against the limits. It is forecast to be £42.1 million at 31st March 2015.

(e) TREASURY MANAGEMENT INDICATORS:

The Treasury Management Code requires the following Treasury Management indicators of prudence:

Upper limit on fixed interest rate exposures;
Upper limit on variable interest rate exposures;
Upper and lower limits for the maturity structure of borrowing;
Total principal sums invested for periods longer than 364 days.

Interest Rate Exposures: It is recommended that the Authority sets upper limits on its fixed and variable interest rate exposures as a percentage of its net outstanding principal sums as follows: -

Upper Limits on Interest Rate Exposures		**2015/16**	**2016/17**	**2017/18**
		%	**%**	**%**
Fixed		100	100	100
Variable		50	50	50

This means that the Deputy Chief Executive will manage fixed interest rate exposures within the range 50% to 100% and variable interest rate exposures within the range 0% to 50% for 2015/16.

Maturity Structure of Borrowing: It is recommended that the Authority sets upper and lower percentage limits for the maturity structure of its borrowings as follows. Percentage of projected fixed rate borrowing that is maturing in each period:

	Upper Limit	**Lower Limit**
Under 12 months	50%	0%
12 months and within 24 months	50%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	50%	0%
10 years and above	90%	0%

Total Principal Sums Invested For Periods Longer Than 364 Days: It is recommended that the limit for investments of longer than 364 days be set at £2 million for each of the years 2015/16, 2016/17 and 2017/18.

(f) PERFORMANCE INDICATORS

The Code of Practice on Treasury Management requires the Authority to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the prudential indicators, which are predominantly forward looking.

The Authority will maintain performance indicators for both borrowing and investment, although it must be stressed that the pursuit of higher performance shall not be at the expense of taking undue risks. The indicators for the treasury function are:

- Borrowing - Average rate of borrowing for the year compared to average available.
- Investments – Internal returns compared to the 7 day LIBID rate.

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

(g) TREASURY MANAGEMENT ADVISORS

The Treasury Management service is provided to the Authority by Liverpool City Council. The terms of the service are set out in an agreed Service Level Agreement. The Council employs treasury management advisers appointed under a competitive procurement exercise who provide a range of services which include: -

- Technical support on treasury matters, capital finance issues.
- Economic and interest rate analysis.
- Debt services which includes advice on the timing of borrowing.
- Debt rescheduling advice surrounding the existing portfolio.
- Generic investment advice on interest rates, timing and investment instruments.
- Credit ratings/market information service comprising the three main credit rating agencies.

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

(G) REVENUE FORECASTS

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

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

- Outline the historical background to the current financial plan
- Outline any movement since the previously approved financial plan,
- Outline the underlying assumptions to support forecast,

Background:-

100. Members will recall that in the past few years the Authority's budget forecasts have dealt with significant financial challenges because of government decisions about the funding of Firefighters pensions in 2006 and the poor outcomes of the Comprehensive Spending Reviews of 2007 and 2010 (CSR2007 & CSR2010).

101. Following the financial crisis of 2008, the Government set its spending review for 2010 to reflect major reductions in public expenditure. The spending review dealt with funding for 2011/12 to 2015/16. For the first two years of that period, the Authority suffered cuts at double the national average for fire and rescue services.

102. Following a successful lobby, when a new system for fire and rescue service funding was introduced for 2013/14, Merseyside subsequently received cuts at approximately the same level as all other fire and rescue services in percentage terms (albeit the absolute impact is higher because Merseyside is more reliant on grant than most other fire and rescue authorities).

103. Between 2000 and 2015 the number of Firefighters in the Service has reduced from 1400 to 764.

104. The Authority has already developed and approved plans to cope with the spending review cuts over the 2011/12 – 2015/16 period and has approved £25.6m of total saving options. Of this £6.3m related specifically to the current two year plan for 2014/15 and 2015/16. The key elements of that plan were:-

- A 10% reduction in support staff numbers and overall support costs by £1.5m
- Other technical and back office savings of £1.4m
- Unavoidable savings in the front-line response by 4 station mergers or outright closures and a reduction in Firefighter posts of about 90 delivered by national turnover rates, saving £3.4m

105. The section below summarises the good progress in delivering the total approved saving options to date:-

	2014/15	2015/16	2016/17	2017/18	2018/19
	£'000	£'000	£'000	£'000	£'000
Options Formally Implemented	-20,107	-20,777	-21,094	-20,974	-20,974
Options awaiting some business re-engineering but being delivered in cash terms	-303	-1,103	-4,203	-4,603	-4,603
	-20,410	-21,880	-25,297	-25,577	-25,577

106. The Service is on track to deliver the approved £6.3m of savings specific to the current two year plan as well .

Progress in Implementing Approved Saving Options					
	2014/15	2015/16	2016/17	2017/18	2018/19
	£'000	£'000	£'000	£'000	£'000
2014/15 Budget Approved Savings:					
Options formally implemented into budget	-1,150	-1,878	-2,120	-2,000	-2,000
Approved Saving Options yet to be formally implemented:					
Non Employee Budget review	0	0	0	0	0
10% saving on Non Uniform Establishment	0	-450	-900	-900	-900
Operational Response	0	-350	-3,000	-3,400	-3,400
Value of Saving Options yet to be formally implemented	0	-800	-3,900	-4,300	-4,300
Total	**-1,150**	**-2,678**	**-6,020**	**-6,300**	**-6,300**

The Authority has received recent reports on the progress with the station merger/closure programme and further information is elsewhere on this agenda. Plans are well advanced to deliver the remaining savings. Therefore the Authority's current financial plan has remained on track.

<u>Changes to the currently Approved Plan 2014/15 – 2015/16</u>:-

GRANT

107. The Government funding settlement for 2015/16 has now been confirmed and it is slightly lower than anticipated, £0.210m, mainly as a consequence of a lower CPI factor being applied to uplift business rates as actual inflation was lower than expected. There have also been reductions to reflect the savings that the Authority are expected to realise from new pension contribution rates associated with the implementation of the new firefighters pensions scheme in April 2015. At the time of writing the government has not yet announced what those contribution rates are.

COUNCIL TAX

108. Each district council has now finalised its forecast on the collection fund and council tax base, the position has improved in terms of the overall income yield mainly due to the number of dwelling increasing.

The Districts of Merseyside have set their tax bases 2015/16 and they are shown in the table below:-

District	2014/15 Council Tax Taxbase	2015/16 Council Tax Taxbase	Variance	
	£	£	£	%
LIVERPOOL	91,976.50	94,459.50	2,483.00	2.70%
WIRRAL	87,786.20	89,344.90	1,558.70	1.78%
ST.HELENS	46,715.00	47,808.00	1,093.00	2.34%
SEFTON	76,992.00	78,319.00	1,327.00	1.72%
KNOWSLEY	30,916.00	32,617.00	1,701.00	5.50%
	334,385.70	342,548.40	8,162.70	2.44%
2014/15 Band D Tax Level	70.07	70.07		
Total Income £	23,430,405	24,002,366	571,961	2.44%

The total tax base for the Authority has increased by 2.44%. This means that each £1 of Council Tax the level of income will be greater than that generated in 2014/15 by £8,162.70. The result of this is that the income from the current level of Council Tax is anticipated to higher by £571,961 (this is assumed to be a permanent increase).

This means that the additional income forecast from a just below **2% increase in Council Tax** in 2015/16 is now £0.480m. This plan assumes that increase. (This is expected to be the maximum level of increase before holding a referendum).

The Authority has the option to consider freezing the Council Tax. The Government has announced the availability of a 2015/16 Council Tax freeze grant if authorities agree to freeze their Council Tax for 2015/16 at 2014/15 levels. The grant will be equivalent to 1% of the basic amount of council tax set for 2014/15. For the Authority this would be equivalent to a 2015/16 Council Tax freeze grant, £0.298m. Ministers have agreed that the funding for the freeze grant should be built into the spending review baseline in the future. This gives as much certainty as possible at this stage that the extra funding for freezing council tax in 2015/16 will remain available in future years. A 2% increase in the precept would yield £0.480m and the council tax freeze grant is £0.298m, a difference of £0.182m. However, if the freeze grant was taken-up then:-

- Future council tax increases would be on a lower base and therefore the future precept income yield would be permanently lower

- The freeze grant once it has been included in base formula grant is likely to be subject to reduction in future years, (at best fixed), if public spending is cut as expected.
- It would not reduce the Authority's reliance on grant funding (but rather increase it)

Members are asked to keep to the approved financial plan and increase the Council Tax in 2015/16 by 2%. Central Government has clear expectations that local government should, in their opinion, freeze the council tax.

The Districts of Merseyside have reviewed their collection funds and identified the proportion of any surplus or deficit attributable to the Authority. The results are set out in the table below and show a net surplus of £1,012,448. This impact is a one-off.

District	**2014/2015** Coll fund deficit/(surplus)
	£
LIVERPOOL	-459,974
WIRRAL	-204,349
ST.HELENS	-44,235
SEFTON	-243,890
KNOWSLEY	-60,000
	-1,012,448

The total increase council tax income and collection fund surplus (one-off) is £1.584m.

BUSINESS RATES

109. The Government has also confirmed the value of the Section 31 grants it will pay to offset the loss of small business's rate income as a consequence of various national policies on rate relief for these companies, totalling £0.267m above that assumed in the original budget forecast.

110. Within the Government settlement funding assessment is an assumption around business rate income and in particular the level of local business rates. The Government funding assumes the Authority will receive 1% of local business rates yield estimated at £4.228m in 2015/16. Each billing authority has prepared an estimate of what they believe they will collect and this estimate is £0.095m lower than that assumed in the settlement grant. In addition rating appeals and other changes such as business closures in the year have resulted in a business rates collection fund deficit of £0.235m. Therefore the overall local share of business rates is £0.330m lower than that in the final settlement funding estimate. Overall the movement has seen a net increase in income of £1.323m.

OVERALL IMPACT

111. The overall impact of all these changes is summarised in the table below:-

	£'m
Reduction in Settlement Fund Assessment	0.210
Increase in Section 31 Grants to reflect national discounts on Business Rates	(0.267)
Adjustment for lower local business rate income forecast	0.095
Business Rate Collection Fund Deficit	0.235
Increase in Council Tax Base	(0.583)
Council Tax Collection Fund Surplus	(1.013)
Overall Change	(1.323)

112. The 2015/16 Budget currently only allows a provision for a 1% paybill increase. The 1% includes pay, pensions and employers NI. This represents a significant risk since staff have had a significant period of low or zero pay increases and there is some possibility of pensions cost increases. In particular at the time of writing whilst a valuation of the anticipated cost of the firefighter pension schemes has been conducted the impact of that valuation on employer pension contribution rates has not yet been announced.

113. It is considered therefore that members might wish to set aside the monies arising from the increase in the taxbase (£0.583m) as a hedge against risks of the paybill increasing by more than 1%.

114. In relation to the other net variation (which is mostly one off) it is proposed that the additional £0.740m is added to the capital investment reserve to try and minimise future borrowing as much as possible.

115. **Therefore if the Authority set a precept increase at just below 2% (as assumed in the current plan) then no further savings would be required to set a balanced budget for just 2015/16.**

Future Years

116. In considering prospects for future years the main areas of concern are:

Government Funding

With an election in May 2015; the continuing high levels of public sector debt; and uncertainty over the economic recovery over the next five years it is not surprising that the Government has not issued any indicative grant settlement figures for 2016/17 or future years. All major political parties have committed to tackle the national deficit during the next parliament but it is accepted that the actual level of cuts may vary as there appears to be significant policy approach differences between the parties. In preparing the 2015/16 – 2019/20 five year revenue plan the Service is facing a high degree of uncertainty over grant settlements post 2015/16. **Therefore Officers have taken the view that Government cuts in grant will continue at similar levels to those over the current spending review period**.

Council Tax

117. The plan assumes future council tax increases will be at the current referendum limit of 2%

Pay Bill

118. The plan assumes that pay constraint will continue and that the overall pay bill (including pension costs) will increase at 2% p.a. The Government is currently finalising the proposed employer pension contribution rates for the firefighter pension schemes. The financial plan assumes that any recommendations will have an overall neutral impact.

Other

119. Using the proposed 2015/16 – 2019/20 capital programme to estimate future borrowing provision has been made to cover debt servicing cost and MRP payments that are consistent with the MRP statement in this report.

120. The plan assumes New Dimension funding, £1.1m, will suffer no additional cuts to those already applied and will be maintained at the revised 2015/16 levels. Also that the Section 31 grant to compensate for the capping of business rate increases will continue at the 2015/16 level of £0.267m.

A potential position for future years 2016/17 – 2019/20

121. Having taken account of the assumption set out above the table below sets out a potential financial forecast up to 2019/20. Based on the assumptions savings of up to £13.3 million might be required:-

2015/16 - 2019/20 MTFP

	2016/17	2017/18	2018/19	2019/20
	£'000	£'000	£'000	£'000
2014/2015 Approved Financial Plan	62,889	64,589	66,089	67,589
2015/16 Issues				
Increase in Sec 31 Grant for restricted NNDR increase	-77	-77	-77	-77
Minimum Revenue Provision (MRP) & Interest Payable on loans		250	500	750
Adjust Planned Drawdown from smoothing Reserve to reflect movement in Council Tax yield				
2014/15 Financial Plan Expenditure Forecast	**62,812**	**64,762**	**66,512**	**68,262**
FUNDING				
Government Funding - Settlement Funding Assessment	-34,082	-31,748	-29,898	-28,447
Adjustment for Local Business Rate income forecast from Districts to CLG estimate	0	0	0	0
NNDR Collection Fund (surplus)/deficit	0	0	0	0
Council Tax -				
Base Precept Income	-24,482	-24,972	-25,471	-25,980
Council Tax Base (increase) / decrease	0	0	0	0
Assume **2% rise 2015/16 to 2019/20**	-490	-499	-509	-520
Council Tax Collection Fund (surplus)/deficit				
Updated Income Forecast	**-59,054**	**-57,219**	**-55,878**	**-54,947**
Forecast Net Position (surplus) / deficit	**3,758**	**7,543**	**10,634**	**13,315**
Potential Future Saving To Be Identified	**-3,758**	**-7,543**	**-10,634**	**-13,315**

122. The Authority has already approved a balanced two year plan (2014/15 – 2015/16).

123. There is considerable uncertainty about what will happen to the public finances post the election and how that will impact on local government. However it currently seems likely that there will be continued significant funding reductions.

124. It is difficult to make specific decision to address any financial challenge without more detail and the Authority has adopted an approach whereby

    a. it will only deal with any financial challenge that is known given the uncertainty over future years Government funding settlements.
    b. will seek to lobby the Government to minimise the impact of any changes in any future Comprehensive Spending Review.
    c. It will sensibly prepare contingency plans to deliver additional savings which minimise the impact on operational response

    It will maintain levels of reserves appropriate to the financial risks which will allow time to implement savings required.

(H) Options for Tackling the Future (2016/17 – 2019/20) Financial Challenge

125. Although the previous section identified that the Authority in effect has set a balance budget for 2015/16 that does not require any further savings to be identified (assuming a 2% precept increase is approved), this section of the report considers what areas of the service any future savings will need to be found from if the saving requirement is £13.3m by 2019/20.

126. This section will:-

- Consider the current VFM Principles underpinning decisions on budget saving decisions
- Analyse what budget areas delivered the 2011/12 – 2015/16 savings
- Consider what areas can contribute to the 2016/17 – 2019/20 potential £13m challenge.

127. Before looking at any areas of potential savings it is important to remember that the Authority has agreed a number of Value For Money Principles that have underpinned its approach to budgets and financial plans in recent years. During 2012/13 the principles were reviewed and updated to better reflect the challenges facing the Authority now and in the future. They are:-

Value for Money Principles (Budget Principles):

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

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

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

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

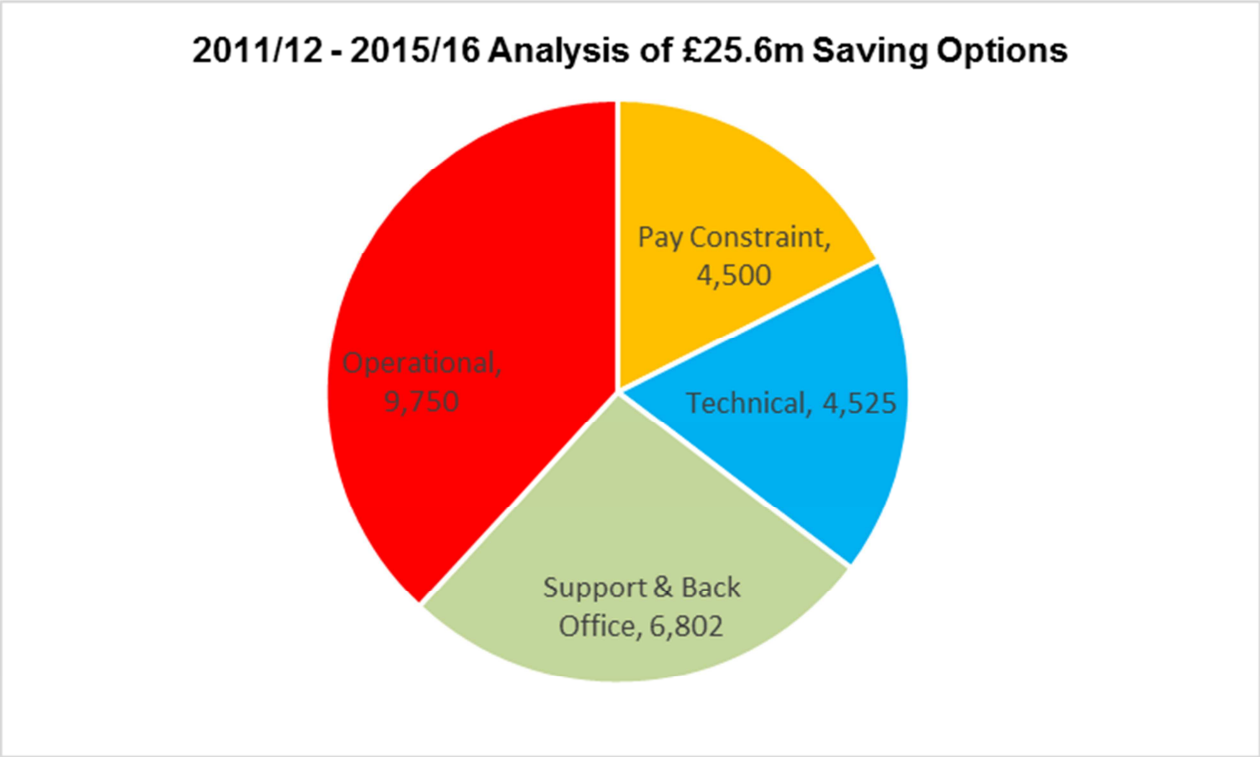
Principle 5 – To allocate resources having considered the impact on our diverse communities and our employees.

128. In applying these principles the Authority has already made large scale budgetary changes and savings. As the Authority faces a further five years of potentially significant financial savings the Authority has very limited room for manoeuvre and these principles may prove difficult to maintain.

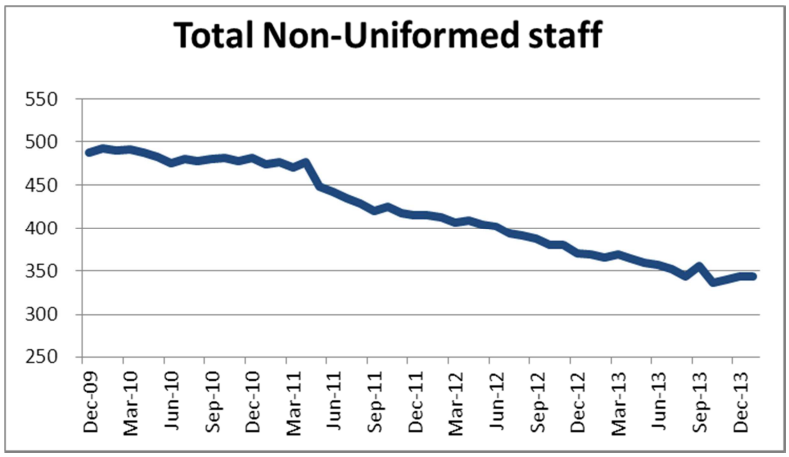
Analysis of Saving Options Already Approved

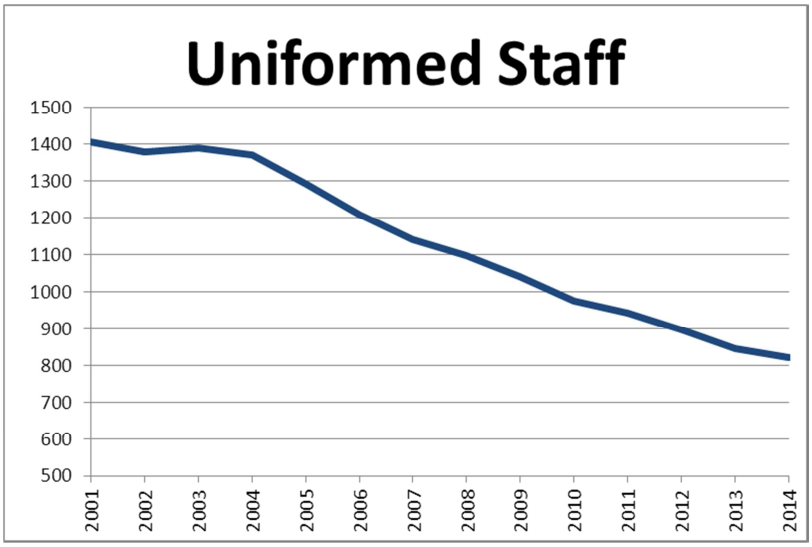
129. The bullet points overleaf and summary pie chart outlines how the £25.577m of saving options approved over the 2011/12 – 2015/16 period have been found:-

a. The number of appliances has been reduced from 42 to 28
b. The number of fire stations is planned to reduce from 26 to 22
c. The number of firefighter post reductions is approximately 200
d. Operational employee savings of £9.750m
e. The number of support staff is planned to fall by 90
f. Support staff and Non-employee saving of £6.802m
g. Annual staff pay rises have been restricted to a 3% in total over this 5 year period (note 2015/16 firefighter pay award still to be announced). Reduction in Financial Plan of £4.500m
h. Technical savings of £4.525m (reduction in non-employee inflation £1.625m; revenue costs associated with capital borrowing of £2.400m; and income generation of £0.500m)



130. The graphs below show how staff numbers have been reduced already.





What areas can contribute to future savings?

131. **Council Tax**:
The Financial Plan assumes a just below 2% council tax increase for 2015/16 and future years which is in line with inflation forecasts. This is expected to be the maximum level of increase before holding a referendum.

The Authority might consider **a higher (above 2%) Council Tax increase.** This would require the Authority to hold a referendum (local vote on its proposals). The advantages of this approach would be:-

- Permanently increased income
- Reduced reliance on grant funding in the mid term
- Potentially avoids cuts in service although the increase would need to be Significant as each additional 1% would generate approximately £0.240m in additional council tax income. As an example a 27% increase (additional 25% above that in the plan) would generate £6.000m towards any future financial challenge.
- The current band d council tax is £70.07, a 27 % increase would increase by £18.92pa to £88.99.
- Future council tax increases would be cumulative on this base

There are a number of practical issues relating to a potential referendum that would make it a risky proposition;

- The Authority has to meet the costs of the referenda – it would need to hold one in each district and get a positive vote in each (Estimate £1m-2m),
- The Authority would have to meet the cost of rebilling if it were not successful (potentially as high as £2m) and would still have to find the required savings to balance the budget,
- There are administrative limitations on the process and campaigning around any referendum which would limit the ability to present a comprehensive argument
- There would be a substantial impact on the taxpayer

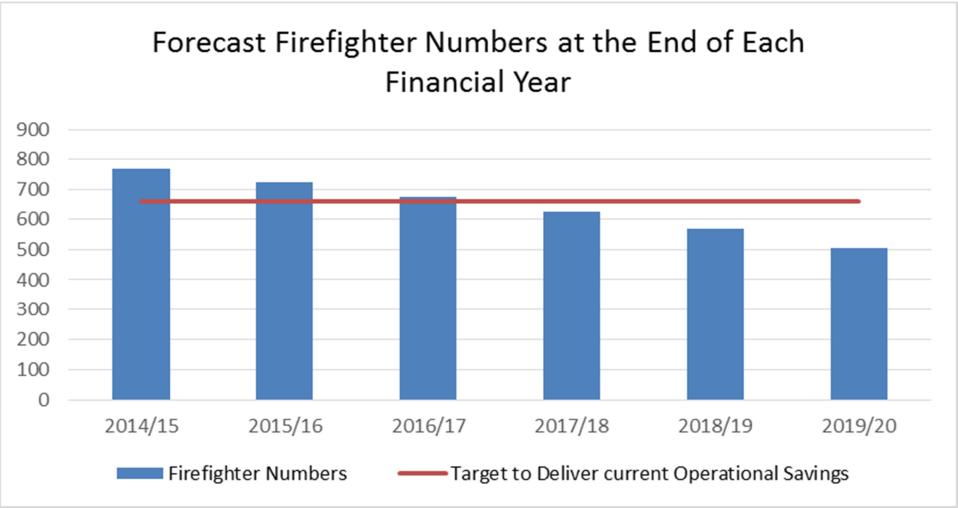
132. **Expenditure**

Given the level of potential savings that may be required and with nearly 70% of the budget relating to employee costs the reality is that reducing staff numbers would almost certainly be required The table below outline the 2015/16 revenue budget over the various types of spend:-

DRAFT 2015/16 Revenue Budget			
	%	£'000	£'000
EMPLOYEE Firefighter pay	49.8%	33,947	
EMPLOYEE Control pay	1.9%	1,299	
EMPLOYEE Non-Firefighter pay	13.0%	8,839	
EMPLOYEE Member payments	0.3%	222	
EMPLOYEE Firefighter Ill Health & Injury Pensions charge	2.7%	1,868	
EMPLOYEE Training & Other indirect costs	1.5%	1,004	
EMPLOYEE	69.2%		47,179
CAPITAL FINANCING (debt interest / MRP)	9.1%		6,226
CAPITAL FINANCING (RCCO/HFSC sals)	1.3%		880
AGENCY SERVICES (Outsourced ICT, PFI Rental & Other)	6.9%		4,673
SUPPLIES & SERVICES	6.0%		4,088
PREMISES	4.5%		3,084
TRANSPORT	2.2%		1,510
CENTRAL EXPENSES	0.8%		518
TOTAL SPEND	100.0%		68,158
INCOME			-6,081
CONTINGENCY FOR PAY/PRICES			1,321
RESERVES			-1,229
NET BUDGET			62,169

133. The Authority would no doubt continue to try and protect the front line as much as possible but again the level of savings is likely to mean further reductions in appliances and a review of fire station numbers and duty system arrangements.

134. The current forecast is that the firefighter establishment will reduce to approximately 670 wholetime equivalents once all the approved saving options have been fully delivered. This is expected to be achieved in 2017. The table below outlines that if no further recruitment took place then by 2019/20 firefighter numbers would be around 500 and this would produce a saving of approximately £6m:-



135. Nearly 10% of the budget is committed to fund revenue costs associated with capital expenditure funded by borrowing. This reflects expenditure already spent so the level of flexibility to drive out further efficiencies is limited. However, the Deputy Chief Executive would continue to consider ways of delivering savings through effective treasury management (using internal cash when available to delay borrowing and other such technical options).

136. It may be possible to drive further savings from non-employee costs however these are often closely linked to the frontline operational service; running costs for fire stations and appliances, uniform and PPE for firefighters.

137. The plan assumes pay awards of 2% from 2016/17, however following a lengthy period of pay constraint pressure is growing for higher pay awards. Each additional 1% would require additional budget of approximately £0.450m.

Conclusion

138. Members have approved a balanced budget for 2015/16 as part of the two year saving plan approved at last year's Budget Authority meeting. Given the level of uncertainty over the future Government funding cuts Members are asked to note the above and direct the CFO to:-

- Develop a lobbying strategy around the next comprehensive spending review to seek to protect as much as possible the fire services budget, and

- Begin planning for the expected savings outlined in the financial plan.

(I) ADEQUACY OF RESERVES AND BALANCES

139. Responsibilities of Chief Finance Officers

140. Under Part 2 of the Local Government Act 2003, the Chief Finance Officer of an Authority is now required to comment on the following matters:

- the robustness of the estimates made for the purposes of determining its Budget Requirement for the forthcoming year;

- the adequacy of the proposed financial reserves.

141. There is then a requirement for the Authority to have regard to the report of the Chief Finance Officer when making decisions on its Budget Requirement and level of financial reserves.

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

143. To make a final judgement on these issues it will be necessary to consider the proposed budget decisions of the Authority in the light of this budget report.

Robustness of Estimate

144. To fully satisfy the Chief Finance Officer any proposed Budget or amendment should therefore:-
    - Be fully based upon the advice of Service Officers (supported by Finance Officers) – or based upon or supported by information the Chief Finance Officer considers reasonable to accept.
    - Provide only for Budget proposals that are fully costed to service level and where the implications – both financial and upon service performance – are estimated and identified.
    - Provide for all known future developments either through direct service Budget allocations or the establishment of specific reserves for such purposes.
    - Provide for an adequate level of Balances and Reserves consistent with the requirements of any Regulation that may be earmarked and/or the Authority's own risk assessment.
    - Provide for the full revenue implications of the Capital Programme.
    - Establish clear targets for income collection in respect of key income streams.
    - Ensure there are no unidentified savings targets.
    - Where appropriate ensure that the consequences of current over and under spending have been taken into account.

Adequacy of proposed Financial Reserves

145. Under the 2003 Local Government Act the Secretary of State may enact Regulations that define certain types of "controlled reserves" and the minimum level

for those Reserves. At the time of preparing this report the Secretary of State has not enacted any such Regulations.

146. However, the 2003 Act still places a requirement upon the Chief Finance Officer to report if the level of reserves is likely to be inadequate. That report should contain comment upon:
    - the reasons for that situation
    - the actions, if any, considered appropriate to prevent the situation arising.

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

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

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

    - an appropriate level was 5% of the forecast Net Operating Expenditure, or

    - that the organisation had a financial risk management process operating which justified a lower level of reserves".

    This is the 'normal' rule for multi-service local authorities.

150. For this Authority a 5% forecast Net Operating Expenditure equates to approximately £3million. The Authority's general revenue reserve is currently £2.000m, however:-

    - The Authority's risk management arrangements have improved. As part of this budget process the Deputy Chief Executive has prepared a financial risk management matrix and also assessed the year on year variation in risk facing the Authority. This takes account of the corporate risk register.
    - The Authority has previously maintained a number of specific earmarked reserves against risk.
    - The Authority is single purpose and does not face as full a range of risks to manage as a multi-purpose authority.
    - The Authority is unlikely to face significant increases in cost because of uncontrollable demand issues (unlike for example Social Services care for the elderly).
    - Members will note that the Authority's revenue reserves have not generally been consumed during the year by overspendings but have been maintained throughout the year.

    Therefore, as the significant risks are known and are being managed or have a specific reserve, the Deputy Chief Executive recommends maintaining the general reserve at its current £2.000m level.

151. Current Reserves:- Based on the latest financial review and known planned future use the Authority's forecast reserves are outlined in the table below:

FORECAST USE OF RESERVES							
	EXPECTED USE						
	Estimate Balance 31.03.15	2015/16		2016/17	2017/18	Future Years	Balance
		Used in 2015/16 Budget	Forecast in year Use				
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Emergency Related Reserves							
Bellwin Reserve	147					-147	0
Insurance Reserve	370					-370	0
Emergency Planning	75					-75	0
Catastrophe Reserve	500					-500	0
Modernisation Challenge							
Smoothing Reserve	1,695	-372	-1,323	646		-646	0
Severance Reserve	600		-600				0
Ill Health Penalty Reserve	440		-220	-220			0
Recruitment Reserve	1,000		-400	-600			0
Capital Investment Reserve	10,786	-882	176	-4,500		-5,580	0
PFI Annuity Reserve	2,225	-49	-51	-100	-100	-1,925	0
Equality / DDA Investment	285		-285				0
Firefighter Safety Investment	800		-800				0
Specific Projects							
Community Sponsorship	4		-4				0
Equipment Reserve	111		-111				0
Contestable Research Fund	25		-25				0
FSD Reserve	6		-6				0
Healthy Living	35		-35				0
Water Rescue Reserve	1		-1				0
Inflation Reserve	500	0	572	0	0	-1,072	0
Ringfenced Reserves							
F.R.E.E. Reserve	41					-41	0
Princes Trust Reserve	279					-279	0
Community Youth Team	53					-53	0
Beacon Peer Project	50					-50	0
Innovation Fund Reserve	170					-170	0
Regional Control Reserve	0					0	0
Energy Reseve	84	74				-158	0
St Helens District Reserve	6					-6	0
New Dimensions Reserve	793					-793	0
Total Earmarked Reserves	**21,081**	**-1,229**	**-3,113**	**-4,774**	**-100**	**-11,865**	**0**
General Revenue Reserve	**2,000**	**0**	**0**	**0**	**0**	**0**	**2,000**
Total Reserves	**23,081**	**-1,229**	**-3,113**	**-4,774**	**-100**	**-11,865**	**2,000**

152. The latest financial review report CFO/005/15 identifies a 2014/15 forecast revenue underspend which will allow the Authority to increase its capital investment reserve by a further £0.4m. The current estimated reserves as at 31.03.15 are:-

• Ringfenced Reserves (not available for general spend)	£1.5m
• Earmarked Reserves (created to fund future projects or as a resource to meet some potential future spend)	£19.6m
• General Fund Reserve (required to cover unexpected events)	£2.0m
	£23.1m

Approximately £19.6m of earmarked reserves might be seen as available, however, £11.6m of this has already been committed to fund approved current and future capital investment, including the construction of new stations as part of the station merger initiative and controlling the level of borrowing to deliver the approved revenue debt servicing savings. Also £1.1m is required to cover insurance and catastrophe risks; £0.4m of the smoothing reserve is required to balance the 2015/16 budget; and £2.2m is required to smooth out the future PFI unitary charges over the remaining contract years. This leaves £4.3m of earmarked reserve to consider. Although this would appear relatively high it reflects the level of risk associated with the current financial plan and the severity of cuts imposed on the Authority for 2015/16 and beyond. The £5.4m earmarked reserves are:-

£'m	
Severance Reserve	0.6
Recruitment Reserve	1.0
Firefighter Safety	0.8
Inflation Reserve	1.1
Ill Health Cost	0.4
Equality / DDA	0.2
Insurance & Catastrophe	1.1
Other	0.2
	5.4

153. Based upon assumptions that; the Authority will adopt all the savings identified and their attendant risks; that the Authority needs a buffer to give it time to make changes required; and, in order to avoid compulsory redundancy if possible the Deputy Chief Executive recommends the Authority hold the £4.3m identified above in reserves at the start of the financial plan.

Members should bear in mind that reserves and balances should only be used to finance one-off expenditure. If such monies are used to fund ongoing revenue expenditure without taking action to reduce underlying expenditure, the Authority would find itself facing the same deficit in the next and future years but without reserves available to finance it. This is underlined by the District Auditor's 'Golden Rule' - that "one off" revenue reserves should not be used to support 'ongoing' revenue expenditure.

Review of Reserves and Balances

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

(J) BUDGET TIMETABLE & RESOLUTION

155. There is a legal requirement for the Authority to set a balanced budget and decide its level of precept before 1st March 2015. The Authority meeting is now invited to:

- Confirm the financial plan set out in Appendix D, approve the budget requirement of £62.169m for 2015/16 as outlined in Appendix D.
- note that the Authority's council tax base for 2015/16 is 342,548.40, being the aggregate of the tax bases calculated by the Districts.
- approve the following amounts calculated in accordance with Sections 42a to 49 of the Local Government Finance Act 1992:-

Calculation of Aggregate Amounts Under Section 42a (2) and (3) of the Local Government Act 1992 (Updated in the Localism Act 2011)					
			Gross Expenditure 2015/16	Gross Income 2015/16	Estimate 2015/16
			£'000	£'000	£'000
(A)	sec 42 (2) (a)	Service Budget	69,593		69,593
(B)	sec 42 (3) (a)	Income		-6,195	-6,195
		Reserves Movement:			
(A)	sec 42 (2) (c)	Contribution to reserves	74		74
(B)	sec 42A (3) (a)	Contribution from reserves		-1,303	-1,303
		Budget Requirement	69,667	-7,498	62,169
(B)	sec 42A (3) (a)	Spending Funding Assessment		-37,004	-37,004
(B)	sec 42A (3) (a)	Local NNDR Estimate Adjustment		95	95
(B)	sec 42A (3) (a)	Collection Fund Deficit / (Suplus)		-778	-778
(C)	In accordance with Sec 42A (4), aggregate of (A) over (B)	**Precept Requirement**			**24,482**
		Tax Base			**342,548.40**
		Basic Tax Amount At Band 'D'			**£71.47**

156. The valuation bands calculated by the Authority in accordance with Section 47 (1) of the Act, as the amounts to be taken into account for the year in respect of categories of categories of dwellings listed in different valuation bands:

2014/15	2015/16	Property Band		Increase	
	£			£	%
£46.71	£47.65	For properties in Band	A	0.94	2.01
£54.50	£55.59	For properties in Band	B	1.09	2.00
£62.28	£63.53	For properties in Band	C	1.25	2.01
£70.07	£71.47	For properties in Band	D	1.40	2.00
£85.64	£87.35	For properties in Band	E	1.71	2.00
£101.21	£103.23	For properties in Band	F	2.02	2.00
£116.78	£119.12	For properties in Band	G	2.34	2.00
£140.14	£142.94	For properties in Band	H	2.80	2.00

157. The Authority calculates the precept amounts payable by each constituent district council pursuant to Section 48 of the Act as follows:-

District	2015/16 Council Tax Taxbase
	£
LIVERPOOL	94,459.50
WIRRAL	89,344.90
ST.HELENS	47,808.00
SEFTON	78,319.00
KNOWSLEY	32,617.00
	342,548.40

158. The precept payments are to be made by 10 equal instalments on or before the following dates:-

21st April 2015
29th May 2015
6th July 2015
11th August 2015
17th September 2015
23rd October 2015
30th November 2015
8th January 2016
15th February 2016
17th March 2016

Equality and Diversity Implications

159. Future reports on individual aspects of the savings required to balance the budget will be accompanied by EIAs.

160. The financial plan makes provision for the required investment to ensure the Authority meets and exceeds its Equality and Diversity requirements in addition to work carried out by all staff and teams.

Staff Implications

161. The relevant consultation will take place as and when the plans are drawn up to deliver the required staffing change to deliver the reduction in support staff and firefighters.

Legal Implications

162. The Authority must set a balanced budget and decide its level of precept before 1st March 2015.

Financial Implications & Value for Money

163. See Executive Summary

Risk Management, Health & Safety, and Environmental Implications

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

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

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

BACKGROUND PAPERS

CFO/011/14 "MERSEYSIDE FIRE & RESCUE AUTHORITY BUDGET & FINANCIAL PLAN 2014/2015 – 2018/2019" AUTHORITY 27 FEBRUARY 2014.

CFO/005/15 "FINANCIAL REVIEW REPORT 2014/15 APRIL TO DECEMBER REVIEW" AUTHORITY 26 FEBRUARY 2015

GLOSSARY OF TERMS

MFRA **M**erseyside **F**ire and **R**escue **A**uthority

MFRS	**M**erseyside **F**ire and **R**escue **S**ervice
CFR	Capital Financing Requirement – measures the amount of capital spending that has not yet been financed by capital receipts, capital grants or contributions from revenue income. It measures the underlying need to borrow for capital purpose, although this borrowing may not necessarily take place externally (use of available cash etc).
CSR07, 10, 13	Government comprehensive spending review to identify support for the public sector over 2 to 3 year period
MRP	MINIMUM REVENUE PROVISION - An amount set aside from revenue towards the repayment of loan debt.
RESERVES	Amounts set aside to meet future contingencies but whose use does not affect the Authority's net expenditure in a given year. Appropriations to and from reserves may not be made directly from the revenue account.
UNSUPPORTED BORROWING	No Revenue Support Grant to cover the costs associated with borrowing and the Authority must earmark revenue funds to cover these costs.