HAMPSHIRE FIRE AND RESCUE AUTHORITY

Purpose: Approval

Date **4 December 2019**

Title **2020/21 BUDGET UPDATE**

Report of the Treasurer

EXECUTIVE SUMMARY

1. This report is to provide an update to members of the current financial position for the 2019/20 Revenue Budget and an update on the 2020/21 budget setting process.

2. An underspend of £0.447m is currently forecast against the 2019/20 budget as detailed in paragraphs 15-17 below.

3. No Medium Term Financial Plan (MTFP) has been presented to the HFRA this year, as we were awaiting the results of a multi-year Spending Review that was due to take place over the Summer. Given the national political situation and ongoing Brexit issues only a one year Spending Round was announced and the details of this are reflected in this report.

4. The latest reported forecast for 2020/21 that is available is from the September 2018 MTFP and anticipated a deficit of £1.8m. However, £0.7m of that was found as part of the 2019/20 budget setting process and it is possible that the remaining shortfall will be covered by higher than forecast Government Grant, increases in the Council Tax Base and some reductions in the estimated requirements for inflation.

5. The precept increase was forecast at 1.99%, and this is in line with the limits set out in the Spending Round, albeit that the Government will consult on the referendum limit in due course. Given the continuing uncertain financial future it is recommended that the precept be increased by the maximum allowed in 2020/21.

6. There has also been a favourable change in the funding position for the Hampshire Local Government Pension Scheme (LGPS) which will impact on our forecasts for next year and this report sets out a proposed strategy for dealing with this.

7. Given the ongoing uncertainty about future grant settlements and the fact that detailed figures for next year will not be announced until December, it is proposed that an 'interim' financial plan be brought forward to the Authority when it sets the budget and precept for 2020/21 in February next year.

BACKGROUND

8. The current financial year represents the final year of the current Spending Review period, beyond this time, no grant figures were available, albeit that a Spending Round was expected in Summer of 2019. Given this position, it was decided to delay the production of the Medium Term Financial Plan (MTFP) which is normally reported in September each year, to February when it was expected that we would have a further multi-year settlement with detailed figures for HFRA.

9. Members will be aware that given the national political situation surrounding Brexit, it was decided to do a single year Spending Round for 2020/21 in September 2019, but which provided more financial certainty for the public sector earlier than would normally be the case. The Spending Round was announced on 4 September and whilst there was significant information released for Local Government, there were only a few key messages for Fire:

   - Real terms increase in grant funding (the Home office Departmental Expenditure limit has increased by over 6% but we do not know how much of this will come to Fire);
   - A continuation of the Pension Grant at the same levels as 2019/20 – a significant issue for all Fire Authorities;
   - A core council tax referendum limit of 2%, a reduction from the 3% level that had been allowed over the last two financial years.

10. Whilst this provides some level of certainty for 2020/21 it means that even by February 2020, the Authority will have no visibility of its financial position beyond this time and it may therefore be necessary to consider an ‘interim’ financial plan to deal with this exceptional position, which will be considered in February next year.

11. Turning to the budget for 2020/21, the plan presented to the HFRA in September 2018 showed a predicted £1.8m funding shortfall for 2020/21. That included a £0.7m deficit carried forward for 2019/20, which was found through the budget setting for 2019/20 and this therefore reduces the on-going deficit to £1.1m.

12. The budget setting process is currently underway, which will review all budget lines with the aim of ensuring that they are valid and accurate and will remove any excess funding that is held within departments.

13. The MTFP included a reduction in grant of around £700,000 in 2020/21 and therefore, even allowing for a 2% increase on the 2019/20 figure would provide additional funding of £840,000 compared to the forecast position. It is anticipated that this change together with other favourable movements in the forecast, will hopefully enable a balanced budget to be set for 2020/21.

14. Budget monitoring is carried out through the year, with quarterly forecasts being presented to Executive Group and the HFRA. The forecast position as at 30th September 2019 is for an underspend of £0.447m.

2019/20 QUARTER 2 BUDGET MONITORING

15. The table below shows the budget monitoring for 2019/20 as at 30 September 2019.

	2019/20 Current Budget Quarter 2 *£'000*	2019/20 Forecast as at end Quarter 2 *£'000*	Variance Underspend / (Overspend) *£'000*
Employee costs	54,134	53,266	868
Premises	5,938	6,031	(92)
Transport	1,545	1,786	(241)
Supplies & services	12,423	12,461	(38)
	74,040	**73,543**	**497**
Income	(1,464)	(1,452)	(11)
Specific grant	(2,473)	(2,434)	(39)
Interest payable / (receivable)	578	578	0
	70,682	**70,235**	**447**
Cont'n to/(from) Capital Payments Reserve	1,358	1,358	0
Cont'n to/(from) Transformation Reserve	(1,866)	(1,866)	0
Cont'n to/(from) other reserves	438	438	0
Net Cost of Service	**70,612**	**70,165**	**447**

16. The main points to note are:

    (a) There is a significant underspend on employees due to vacant posts following re-structuring. These posts are now being recruited to and this underspend is expected to reduce over coming months.

    (b) There is an overspend of £92,000 on Business Rates, particularly at Basingstoke Fire Station caused by higher than expected increases on the charges, this will be corrected as part of 2020/21 budget setting.

    (c) The £241,000 overspend on Transport is mainly caused by two factors. Firstly, the travel cost of temporary postings for firefighters. This is being addressed and a new process is now in place to reduce this cost. And secondly, an overspend on vehicle maintenance, including the legislative changes for replacement of tyres on appliances which has needed to be brought forward causing higher spend in this year.

17. The current forecast is a lower underspend than in recent years, this is due to the restructures now having been made and the budgets for savings removed. Posts are planned to be filled during the year and the Service should be running in line with the new operational structure.

RESERVE FUNDING

18. One of the key features of the HFRA MTFP has been the ability to build in recurring contributions to reserves at the same time as reducing spend in response to funding reductions. This ensures that funding is available in the future for major spend on capital investment and equipment refresh etc. The reserves that we hold are for specific purposes and are not available to temporarily prop up revenue expenditure unless that is part of a deliberate strategy.

19. An updated Reserves Strategy that explains the purpose of the reserves we hold and their planned usage will be presented alongside the budget report in February. This is an important part of our financial planning and is one of the key reasons that HFRA is in the strong financial position that it is today.

20. In line with this strategy, the budget for 2019/20 includes a contribution of £600k towards equipment replacement, which is due to increase to £750,000 next year and is part of the existing MTFP forecast. This was agreed as a way of planning for the replacement of significant equipment and has made a significant difference to the ability of the Technical Services team to plan for future equipment replacement.

21. As part of the ICT Transformation Project, it was agreed that there would be an annual contribution to reserves to cover future replacement costs. However, no specific amount was approved and contributions are not currently being made. As ICT becomes more important to the operational effectiveness of service, it has become clear that a significant annual contribution to reserves will be needed to allow for future replacement programmes.

22. It is therefore proposed that an annual contribution of £0.5m be made to the ICT Reserve and depending on the overall budget position for next year that this is built into the revenue budget from 2020/21 onwards. If it is only possible to include a smaller amount due to the overall financial position then the intention would be to increase the contribution in future years until we can reach the £0.5m target.

CFA FUNDING

23. The new CFA for Hampshire and the Isle of Wight has been approved by the Home Secretary and is now awaiting ratification of the Statutory Instrument, expected in March 2020, which is later than the previously expected date of September 2019.

24. This has meant a delay to the creation of the new CFA from April 2020 to April 2021. Work has been carried out to assess the effect that this delay will have on the implementation costs. The forecast is that between a further £265,000 and £305,000 of funding will be required as a result of the delay.

25. Most of the additional costs relate to the extension of the programme and project resources employed on the project and additional business readiness activity that will need to be undertaken over the extended timeframes. The Authority is asked to approve up to a maximum of £305,000 of additional project funding to be met from the Transformation Reserve.

FORWARD BUDGET 2020/21

26. An interim financial plan will be presented to the Authority in February 2020 once there is more certainty around the detailed figures for 2020/21, in the meantime, the planning assumptions for the 2020/21 budget are detailed below.

Precept

27. In the September 2018 MTFP, a precept increase of 1.99% had been included within the Forecast. No firm referendum limit has been set for 2020/21 as yet, however, the Spending Round indicated that a core council tax referendum limit of 2% will be consulted upon. Given the uncertain financial future it is recommended that the Authority increase council tax by the maximum amount permissible for 2020/21, albeit that this is subject to final confirmation at the Budget Setting Authority planned for February 2020.

28. The total precept received is also affected by the council tax base, which is the total number of dwellings paying the precept within Hampshire. Due to on-going demands for more housing, this figure has increased year on year for many years, but the increase has varied significantly. An increase of 1.0% had been built into the MTFP, but estimates have now been received from the precepting authorities which indicate a higher increase at around 1.5%. This increase will therefore contribute around £220,000 to any remaining shortfall for 2020/21.

Service Delivery Redesign (SDR)

29. The operational changes were made for the SDR programme ready for April 2019 and the new structure has been in place and working across the Service since that time. Most savings were therefore removed from the 2019/20 budget, however there is a further £404,500 is still to be removed, which will happen as part of 2020/21 budget setting. This will bring the total programme saving for SDR to £4.1m.

Zero Based Budget

30. As part of the budget setting process, a version of zero based budgeting is being carried out across the organisation. This is an annual process and will be on-going, to ensure that all budgets are as accurate and relevant as possible.

31. This process involves all budget lines being reviewed to ensure that they are valid and of an appropriate amount. This can result in individual budget lines being increased, reduced, removed or added, but it is expected that the final result will be an overall reduction or will be used to prop up areas where the budget is not representative of normal activity.

Pay Inflation

32. An inflation rate of 2.5% has been used for both professional services colleagues and firefighters for 2020/21. The 2019 increase for Firefighters was recently agreed at 2%, however, discussions are on-going about future increases, with the Fire Brigades Union pushing hard for significantly higher increases in future years. The impact of the 2019 award is a saving of £192,000 on the budget going forward that will be taken into account as part of the detailed budget preparation.

Hampshire LGPS

33. Members will be aware that non firefighting staff are able to join the Local Government Pension Scheme (LGPS) which in Hampshire is managed by the County Council. Unlike the firefighters pension scheme, the LGPS is funded, in that it is backed by a separate fund that is designed to meet the future liabilities for pension payments through member contributions and investment returns.

34. The fund is re-valued every 3 years and for many years there have been significant deficits in the fund that have required increased contributions from employers to try to close the deficit. In 2019/20 HFRA is paying a future service rate of 16.1% of pay together with an annual deficit contribution of around £760,000.

35. In 2016 the fund was around 81% funded, meaning that there was a deficit that needed to be recovered from employers over an extended period. The initial high level results for the 2019 valuation indicate that for ‘scheduled bodies’ (of which we are one) the fund is almost 100% funded following an improvement in investment returns over the period and a slow down in the increases in life expectancy.

36. The higher funding level has also enabled the County Council as administering authority to move to individual employer contribution rates rather than a grouped rate which has been a unique feature of the Hampshire Pension Fund for many years, but is no longer fit for purpose given the complexities around pensions generally and the outsourcing of functions across the local government sector.

37. In terms of the financial impact of the funding level, we expect the future service rate for HFRA to be in the region of 16.8% going forward (although this will not be confirmed until later), which will mean that we need to find approximately £135,000 per annum to provide for this increase (other employers have rates of up to 19.5%). However, the higher funding level does provide the opportunity to reduce the past deficit payments that we are currently making. After allowing for the increase in the future service rate, there will be a net saving in the past deficit contribution of around £625,000 per annum.

38. Whilst this is very positive, it must be set against the potential risk that with the uncertainty of Brexit and the wider impact on the national economic climate, the fund could fall back to previous levels by the next triennial valuation in 2022. If the Authority were to take this revenue saving into its baseline funding now, and the fund were to decline over the period it could mean finding extra recurring revenue money at that stage on top of any further savings that are required to balance the overall budget.

39. With this in mind, and considering the lack of information on our financial position past 2020/21, it is recommended that the net saving of £625,000 per annum arising from the favourable 2019 Pension Fund valuation be used to create a Grant Equalisation Reserve in the intervening period, to help smooth any future reductions in grant that may be announced, giving us the time and capacity to implement savings in a planned way. This can obviously be reviewed following the multi-year Spending Review due to take place next year, that will inform our MTFP going forward.

40. On a related item, the move to individual employer contribution rates also provides the opportunity for employers to make pre-payments to the fund to benefit from the additional investment returns that this may yield (which should far exceed the rates available in the market). This report therefore seeks delegated authority for the Treasurer to make pre-payments of contributions (up to three years' worth) and to pay off any residual deficit at the end of this financial year, if it is considered financially beneficial to do so (detailed proposals for pre-payments are due to be released by the fund shortly).

CAPITAL

41. The Capital Programme is currently fully funded through to 2021/22, although in later years the programme makes general assumptions around the level of spend required for vehicle replacement, in line with previous years' requirements.

42. As capital grant is no longer received from government, all funding for capital expenditure must come from capital receipts, borrowing, reserves or directly from revenue (known as Revenue Contributions to Capital Outlay or RCCOs).

43. RCCOs have been increased over recent years in order to bring them to £3.905m, which is the level needed to fund the on-going business as usual requirements of the capital programme (i.e. excluding major investment decisions such as new stations). This figure has therefore now been built into the base budget as RCCO and will become a regular contribution, which will be reviewed in line with future vehicle and property strategies.

44. The table at **Appendix A** shows the expected capital spend and provides the funding plan over the coming years.

TREASURY MANAGEMENT

45. The mid-year Treasury Management Report is attached at **Appendix B**. It provides an update of the Authorities return on investment as at 30 September 2019.

46. In line with the CIPFA code this has to be reported to the Authority.

SUPPORTING OUR SERVICE PLAN AND PRIORITIES

47. Ensuring that funding is appropriately accounted for is vital for all public sector organisations. Good budget management in the past has allowed underspends to be achieved, which will help to fund the Service priorities and enable key changes required to make the budget reductions at the same time as service improvements.

CONSULTATION

48. The Authority undertook a major consultation process during 2015 that sought residents and stakeholders' views about the proposed changes arising from the Risk Review as well as other issues around budgets and council tax levels. The most relevant point to note for this report is that the majority of respondents were happy to see a rise in council tax in order to protect services provided by the Authority.

49. Further consultation is expected to take place with business and Unions as part of the budget setting process for 2020/21.

RESOURCE IMPLICATIONS

50. This report deals with the financial planning and budget setting arrangements for the Authority

LEGAL IMPLICATIONS

51. There is a legal requirement to set a balanced budget and council tax precept each year prior to the 1st March. This report forms part of the planning and governance associated with that decision making process.

EQUALITY IMPACT ASSESSMENT

52. The setting of the overall budget in itself does not have a direct impact on people but where specific proposals (such as savings or new spend) are proposed these will be subject to impact assessments and consultation in line with existing policies.

OPTIONS

53. There are no options for consideration within this report, although budget setting and forecasting by its very nature means that assumptions are made around several variables that can be changed over time.

RISK ANALYSIS

54. The Authority has an established process for planning ahead to meet financial targets. This has helped considerably in managing the reductions in Government grant as set out in this report.

55. The current savings programme has progressed according to plan but development and implementation of a new savings programme will need to be kept under review and will be considered in February next year following the update of the Integrated Risk Management Plan and the announcement of grant figures for 2020/21.

56. The lack of information past 2020/21 is a concern for the Authority and there continues to be a high probability of a budget deficit in future years which will require reductions across the Service and increases in council tax. The Service continues to consider options as to how a shortfall could be overcome, including examining other potential income sources. However, as a backstop position, the Authority has sufficient reserves and makes substantial contributions to reserves each year, thereby mitigating this risk. The creation of a Grant Equalisation Reserve as set out in this report will further mitigate the potential risks faced.

CONCLUSION

57. It is recommended that the Authority approve the assumptions made within this report, which will be used as the basis for 2020/21 budget setting.

RECOMMENDATIONS

58. That Hampshire Fire and Rescue Authority agree with the principle of setting the precept at the maximum level without breaching the referendum limit, subject to final decisions by the Authority in February next year.

59. That the Hampshire Fire and Rescue Authority approve an annual contribution of up to £0.5m into the ICT Reserve dependent on the eventual budget position in February.

60. That additional funding of up to £305,000 be approved from the Transformation Reserve for CFA preparation costs as a consequence of the additional years delay in implementation.

61. That the estimated net annual saving arising from the 2019 Pension Fund valuation be contributed to a new Grant Equalisation Reserve in 2020/21 and future years (subject to review following the Spending Review next year)

62. That the mid-year review of treasury management activities in Appendix B be noted.

63. That delegated Authority be granted to the Treasurer to make pre-payments of contributions (up to three years' worth) into the Hampshire Pension Fund or pay off any residual deficit amount if it is considered financially beneficial to do so.

APPENDICES ATTACHED

64. Appendix A – Capital Expenditure and Funding
65. Appendix B – Treasury Management Mid-Year Report

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