Appendix G

Section 25 Report from the Chief Financial Officer

Section 25 of the Local Government Act 2003 requires the Chief Financial Officer to report to the Authority when setting its council tax on:

- the robustness of the estimates included in the budget, and
- the adequacy of the financial reserves in the budget.

The Authority is required to have regard to this report in approving the budget and council tax. Section 25 concentrates primarily on the risk, uncertainty and robustness of the budget for the next financial year rather than the greater uncertainties in future years. Given the significance of the previous funding reductions announced to the end of the decade and the delay in the next Comprehensive Spending Review (CSR), this report considers not only the short term position but also the position beyond 2021/22.

Robustness of Estimates in the Budget

The budget setting process within the Hampshire Fire and Rescue Authority (HFRA) has been operating effectively for many years and is based on increasing the budgets each year allowing for pay and price inflation and other marginal base changes in the cost or levels of service.

This year's process has been complicated by the move to a new Combined Fire Authority (CFA) that includes the Isle of Wight and required a slightly different approach for setting the budget.

The first stage took the detailed service budgets and grant and council tax income and combined these into an initial 'base' position for 2020/21. Provisions for pay and inflation increases were applied to this in the usual way together with the impact of past budget decisions that had previously been taken by HFRA. This produced a net budget deficit of £1.001m.

The provisions for pay and price inflation are included within each successive MTFP and these are then refined by the Chief Financial Officer in rolling forward the detailed budget for the next financial year.

In general terms, forecasting is undertaken on a very prudent basis, particularly in respect of allowances for pay and price inflation and increases in the council tax base and business rate income.

Growth pressures are considered corporately and agreed by the Authority and are factored into future budgets on a recurring basis and this process was followed for the new CFA and included some items relating to the combination which were identified in the business case submitted to Government and related to providing adequate resources in the base budget for property maintenance. Other growth pressures around IT and Vehicles were also identified in order to ensure that standards of equipment were consistent across the new CFA.

These growth items added a further £954,000 to the budget and whilst this has had the impact of increasing the deficit it does indicate that a thorough piece of work has been carried out in preparing the estimates for next year.

This work builds on the budgets for the current year and despite Covid-19 budget management within the Authority remains strong as demonstrated by the outturn position each year since funding reductions began and as reflected in the annual opinion of the External Auditors who has in the past given an unqualified opinion on the annual accounts and in securing value for money / financial resilience.

At the end of January 2021 we received the formal audit opinion for 2019/20, which gave an unqualified opinion for the accounts and a positive conclusion for the value for money assessment.

As Chief Financial Officer for the Authority I have a close involvement with the budget setting process, which has been increased this year given the move to the new CFA and I am content that the estimates are robust based on the knowledge we have available to us at this time.

Risks in the Budget 2021/22

In some respects, the significant changes to local government finance since 2010 have changed the profile of risk faced by most public sector organisations. In reality, the biggest financial risks now relate purely to reductions in government funding and government policy. As a Fire and Rescue Authority we do not face demand pressures in the same way as those with social care responsibilities and therefore key cost risks tend to be around pay and price inflation and the impact of pensions. Clearly the current financial year has provided significant financial concerns in terms of the impact of Covid-19 and these items together with other traditional risks are outlined below:

a) **Covid-19 –** The impact of Covid-19 on Fire and Rescue Services has obviously been significant from a response point of view, with the Service and key personnel taking an active role in the command structure for the Local Resilience Forum. Whilst the impact on services has been significant, the additional costs and income losses for Fire and Rescue Services has not been to the same level and current predictions are that the financial impact in the current year will be covered in full by the Covid grant received from the Government. However, at the time of writing this report activity and response levels are at the highest point they have been during the pandemic and costs associated with testing and support to health may mean the grant level is exceeded. It may be possible to bid for additional Government contingency funding to mitigate this risk.

   Of greater concern was the potential impact on council tax and business rate income levels going forward, which could have had a major impact on budget setting for next year. Given the unprecedented position presented by the pandemic, billing authorities have not been able to provide any forecasts of collection fund deficits or council tax base estimates until very late in the process.

   Thankfully, council tax base figures have unexpectedly shown a very small increase compared to last year and there is Government grant to compensate authorities for the fact that they would have normally expected a bigger increase. Furthermore, following the announcement of additional Government support for council tax and business rates losses, the impact of collection fund deficits on the budget setting position for 2021/22 is much less than might have been expected, but are less clear at the time of writing this report than would normally be at this point in the process.

   Looking forward, this still could be an area of concern as Government support for individuals and businesses starts to fall out and the full economic impact of the pandemic is felt, but this will be reflected in the preparations for the budget in future years.

b) **Government Funding and Policy** – The provisional local government settlement announced in December last year included a real terms increase in funding for Fire Authorities and this is reflected in the estimates in this budget setting report and was slightly better than had been included in the forecasts to the Shadow Authority.

   Any other significant changes to funding or policy during the year would have to be covered by contingencies or general balances, but generally once grant levels have been set in the final settlement due in January they do not change, so this is not really an area of concern at this stage.

c) **Council Tax** – The Government have granted additional flexibilities in relation to council tax that allow local authorities with responsibility for adult social care to raise the social care precept by up to 3% on top of referendum limit of 2% for 2021/22.

   Despite lobbying from the sector the Government did not grant Fire Authorities the ability to set a £5 council tax increase (as is the case with Districts) which is disappointing as this would have made a significant difference the finances of the authority going forward.

   Increases in council tax form a key part of closing the predicted budget deficits over time and this report therefore recommends that an increase of 1.99% is applied in 2021/22 in line with the assumptions in the interim MTFP. This increase is recommended as there is still a deficit in the budget for 2021/22 and given the uncertainty of the funding position for future years.

d) **Pay and Price Risk** – The rolled forward budget presented to the Shadow Authority in December contained provision of 2.5% for increases in fire fighter pay together with the full year impact of last year's pay award. Similarly a figure of 2% was included for green book staff.

   Following the Government's announcement that there should be a public sector pay freeze for 2021/22, the provisions for the pay awards have been removed apart from an allowance to cover the proposed pay award for the low paid.

   Should a pay award be granted by the relevant pay bodies (as the Government does not set pay for Firefighters or green book staff) then this will have a negative impact on the budget. This is clearly a risk and any award would need to be met from reserves in the first instance and included in forecasts for the budget in 2022/23 and beyond.

   The impact of price inflation has been considered in setting the budget and it would take a major departure from the Authority's assumptions to create a financial problem that we could not deal with.

e) **Employers Pension Risk** – This was highlighted as major risk in the budget in previous years following a significant increase in employers pension contributions which has been met annually by a Government Grant.

   However, the Government have never confirmed that this grant would be ongoing, instead agreeing the grant on a one-off basis in each budget setting round.

   The provisional local government settlement confirmed the grant once again for 2021/22 and during December a letter was received confirming that this amount will be baselined into future settlements, which is positive news and removes this as a major risk going forward.

f) **Treasury Risk** – The Authority has limited exposure to interest rate risk as most long term borrowing is undertaken on a fixed rate. For many years, the Authority has not been undertaking any new long term borrowing as the capital programme does not require it. However, approvals relating to the funding for the Station Investment Programme require significant prudential borrowing starting from next year and decisions on when best to take out this borrowing will need to be considered to limit the ongoing revenue liabilities that this will create.

   At this stage a prudent approach to the speed of delivery of the programme has been taken and allowances for debt costs have been built in on the same basis but have a limited impact next year. This is therefore a small risk in the budget for next year but will increase as the programme progresses should interest rates start to move.

   On the investments side, the Authority has a very prudent approach to forecasting its investment returns and they also represent a very small part of the overall funding for the budget. The investment strategy protects capital ahead of yield and most of the medium term investments are in products that should return a stable income yield each year.

   There is a further risk relating to the fact that negative interest rates are now a feature of the financial markets, but the Treasury Management Strategy has been amended to cover this risk. In any event the relative level of investment returns compared to the overall budget make this a very minimal risk in any case.

The Adequacy of Reserves

The Authority's policy on general balances is to hold a minimum prudent level which is currently set at £2.5m. This was increased significantly at the beginning of the period of austerity to reflect the potential volatility caused by grant reductions and the need to implement savings programmes. The projected level of general fund balances will be 3.06% of net expenditure at the beginning of 2021/22 and it is considered that this remains a comfortable level. It is worth noting that the Authority has never needed to dip into its general fund balance.

The Authority has two key earmarked reserves that it uses to effectively manage its medium term financial position. The Capital Payments Reserve receives contributions each year and is the major source of funding for the capital programme. The balance on the account mainly reflects the timing differences between planning for capital spend and the profile of capital spend which can be over several years for major projects.

The Transformation Reserve receives regular one off contributions from underspends in the year as well as a regular contribution built into the base budget and is used to pay for transformational change that achieves further savings.

The Authority does however need to be cognisant of the rate of spend on transformation programmes and the extent to which these could be resourced by existing capacity rather than through additional new spending. This is particularly important as the level of the reserve will be greatly reduced by the end of this year.

More recently, the authority has also set up reserves in respect of equipment and ICT replacement in order to provide funding for and to smooth the impact of high cost replacements and refresh in these areas. This change only further strengthens the Authority's financial resilience.

Similarly, following savings arising from the pension contributions towards past deficits in the Hampshire LGPS Pension Fund, a contribution of £625,000 per annum (at least for three years) is being put into a Grant Equalisation Reserve (GER) which is not only being used to balance the budget next year but going forward will help to mitigate some of the risks as outlined above.

As pointed out within the interim MTFP, despite the uncertainty of funding beyond 2021/22, the new CFA is well placed to mitigate the risks that this creates due to the high level of revenue contributions to reserves contained within the base budget (currently nearly £6.3m).

Budget 2021/22 – Conclusion

Given the details outlined above, provided that the Authority considers the above factors and accepts the budget recommendations, including the level of earmarked reserves and balances, a positive opinion can be given under Section 25 on the robustness of the estimates and level of reserves for 2021/22.

The Position Beyond 2021/22

Given the announcement of a one year Spending Round for 2021/22, the Authority is still in the position of not knowing what its financial prospects are beyond a one year planning horizon.

Once the next Comprehensive Spending Review takes place, it is likely that local government and Fire Authority finances will be impacted over this period due to the impact of Covid-19 on Government borrowing and the general economic conditions.

We still await the outcome of the Fair Funding Review and the extension of Business Rate Retention, on which consultation papers have previously been published and it is not known what the impact of this might be on resource levels and distribution methodologies going forward. By December 2021 it is hoped that a multi-year position for funding will be known and a more robust plan can be put in place.

However, given the deficit in the budget for 2021/22 savings plans need to be developed now for implementation before or during 2022/23 and the Chief Fire Officer intends to engage with the new combined service to consider what options might be available for savings, efficiencies and income generation going forward.

Whilst there are risks with the Interim Financial Plan these have been mitigated as far as possible and it would take a significant change in the funding regime to create a scenario which the Authority could not cope with and such a change would have a significantly greater impact on the rest of the sector whose financial position is not as stable as the new CFAs.

Rob Carr
Chief Financial Officer
25 January 2021