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 continued lack of a multi-year settlement, this report considers not only the short term position but also the position beyond 2022/23.

Robustness of Estimates in the Budget

The budget setting process within the Fire Authority 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. For the 2022/23 process, necessary increases to budgets resulting from delivery pressures were identified and robustly challenged by the Executive Group, before being presented to the Fire Authority for initial approval. These pressures are a mixture of strengthening resources in key areas and ensuring that reserve contributions are sufficient to allow for the timely refresh of assets.

The Executive Group also considered the ability of the service to deliver efficiencies, to manage the budget gap and ensure value for money in service delivery. The phasing of these plans has subsequently been reconsidered to ensure that they can be delivered to time while balancing other service pressures. Achievement of these efficiencies will be monitored by Executive Group and reported to the Authority during the next financial year. The rephasing ensures that the efficiency estimates within the budgets are robust and achievable.

Inflation rates are currently significantly higher than they have been for several years and some categories, such as energy costs, are even higher. Price rises are also affecting the capital programme. Inflation at “normal” levels has been allocated to service areas with a central contingency retained for responding to exceptional price rises.

At the end of September 2021 we received the formal audit opinion for 2020/21, 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 in the budget setting process 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 2022/23

The biggest financial risks relate to the uncertain medium term financial position of the Authority and the risk that Government funding may reduce. In addition, pay and price inflation remain significant risks to the financial position of the Authority. Although the immediate financial risk presented by Covid-19 has reduced, the risk of the impact of further waves and the medium term economic impact remain.

a) **Government Funding and Policy.** The provisional local government settlement was announced in December 2021 and included a small ongoing increase and a more significant one-off increase in the funding for Fire Authorities. This is reflected in this report and was slightly better than had been included in the December Budget Update report.

   Any other significant changes in year would need to be covered by contingencies or general balances, but generally grants do not change once the settlement has been announced, so for this year this is not an area of concern.

b) **Council Tax.** The Government have granted additional flexibilities to the eight Fire Authorities with the lowest council tax rates. An increase of the maximum amount (£5 or 7.10%) is recommended. This increase allows continued investment in assets and the inclusion of a prudent level of contingency. Along with the efficiencies being delivered it allows the budget gap to be closed, leaving only a modest gap in future years based on prudent assumptions about future costs and funding.

   Were the opportunity to raise Council Tax by £5 not taken, it would be necessary to explore options for savings, including potential service reductions.

c) **Pay and Price Risk. This** risk is greater than normal as price inflation has increased significantly in recent months. A specific price inflation contingency has been built into the budget to mitigate this risk. Budgets for estimated green and grey book pay awards for next financial year have been built into the budget. If pay awards exceed assumed amounts then this will become a pressure on the revenue budget. Price inflation is also impacting on the capital programme. To respond to these greater risks, an additional contingency of £0.5m has been included within the budget.

   In light of these mitigations it would take a major departure from the Authority's assumptions to create a financial problem that we could not deal with.

d) **Treasury Risk.** ~The Authority has limited exposure to interest rate risk as most long term borrowing is undertaken on a fixed rate basis. As a result of the significant prudential borrowing required for the Station Investment

Programme, the Authority will need to start borrowing externally. Decisions on when best to take out this borrowing will need to be considered to limit the ongoing revenue liabilities that this will create.

Sufficient allowances for the costs of this additional borrowing have been built into the budget for the coming year.

On the investment 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 projects 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.

e) **Covid-19.** The financial impact of the Covid-19 pandemic on the Authority has been limited, with additional costs currently covered by grant funding. Grant funding is now largely exhausted so there is a risk that further costs may need to be covered from existing resources. However, indications are currently that the costs of further support to partners will be covered either by the partner or by additional grant.

At the time of writing, Council Tax income has held up although Business Rate income is still based on estimates as billing authorities have not yet provided full information. The full economic impact of the pandemic is not yet clear so this remains a concern for future years.

<u>The Adequacy of Reserves</u>

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 2.87% of net expenditure at the beginning of 2022/23 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 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 accumulation of funds to be used for the Vehicle Replacement Programme which has experienced delays over recent years.

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 transformation and change that achieves further savings and efficiencies.

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 replacement and refresh in these areas. This change only further strengthens the Authorities financial resilience.

Similarly, following savings arising from the pension contributions towards past deficits in the Hampshire Local Government Pension Scheme Pension Fund, a contribution of £625,000 per annum is being put into a Grant Equalisation Reserve. This was used to balance the budget in 2021/22 and there is a planned use of this reserve to balance the budget in future years as set out in the MTFP.

As outlined elsewhere in this report, despite the uncertain financial position in the medium term, the Authority is well placed to mitigate the risks that this creates due to the high level of revenue contributions built into the base budget (currently nearly £6.7m).

Budget 2022/23 – Conclusion

Provided that the Authority considers the above factors and accepts the budget recommendations, especially the recommendation to increase Council Tax by the proposed maximum allowable amount, a positive opinion can be given under Section 25 on the robustness of the estimates and level of reserves for 2022/23.

The Position Beyond 2022/23

Given the announcement of a further one year spending round for 2022/23 the Authority is still in the position of not knowing what its financial prospects are beyond a one year planning horizon.

We still await the outcome of the Fair Funding Review and the decision about any potential revision of the Fire funding formula. It is not known what the impact of these may be on resource levels and distribution methodology is going forward. The ongoing economic impact of the Covid-19 pandemic and impact of this on the public finances is still unclear.

Efficiencies have been planned as part of the budget setting for 2022/23 and the MTFP. Further efficiencies are likely to be required in the medium term.

Whilst there are risks within the Medium Term 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.

Rob Carr
Chief Financial Officer
1 February 2022