TYNE & WEAR FIRE AND RESCUE AUTHORITY **ITEM NO. 6**

MEETING: 5th NOVEMBER 2018

SUBJECT: BUDGET PLANNING FRAMEWORK 2019/2020

JOINT REPORT OF THE CHIEF FIRE OFFICER AND CHIEF EXECUTIVE (CLERK TO THE AUTHORITY) AND THE STRATEGIC FINANCE MANAGER

1 Purpose of Report

1.1 This report sets out the main considerations in drafting the Revenue Budget 2019/2020 and the longer term financial planning for the Authority which includes:

- Identifying the key factors influencing the development of the Authority's financial plans into the medium term and sets out specifically the Budget Planning Framework for 2019/2020;
- Providing an update on the current Medium Term Financial Strategy and sets out the headlines and context for the Medium Term Financial Strategy 2019/2020 to 2022/2023 which will be formally considered later in the budget cycle; and
- Providing an update on performance against the four year Efficiency Plan 2016/2017 to 2019/2020.

2 Medium Term Financial Strategy 2018/2019 to 2021/2022

2.1 The Medium Term Financial Strategy 2018/2019 to 2021/2022 was approved by Authority in February 2018 as part of the 2018/2019 budget setting process. The plan is continually updated to reflect changing circumstances and latest known information. The Medium Term Financial Strategy will be kept under review throughout the budget process and updated as required, with a full Medium Term Financial Strategy 2019/2020 to 2022/2023 presented to Authority in February 2019.

2.2 The table summarises the slightly updated Medium Term Financial Strategy:

	2018/19 £m	**2019/20 £m**	**2020/21 £m**	**2021/22 £m**
Government Grant Reductions	1.059	0.548	0.387	0.249
Spending Pressures	2.740	1.838	1.183	1.128
Total	**3.799**	**2.386**	**1.570**	**1.377**
Less IRMP estimated savings	(0.924)	(0.106)	0	0
Less Council Tax and Business Rate growth*	(1.233)	(0.528)	(0.713)	(0.733)
Less budget efficiencies	(0.948)	(0.130)	(0.127)	0
Funding Gap in year	**0.694**	**1.622**	**0.730**	**0.644**
Cumulative Funding Gap	**0.694**	**2.316**	**3.046**	**3.690**

**Assumptions in the Table assume a 2.99% increase in the precept in 2019/20 and a 1.99% increase thereafter and 1% growth in the base each year for both council tax and business rates*

2.3 Based on the best information available at this time, the Authority is projected to be facing a cumulative funding shortfall of £3.690m by the end of 2021/2022. The amount of the budget deficit within the Four Year Efficiency Plan period which ends 2019/2020 has increased to £2.316m from an original estimate of £1.8m. This position represents a significant challenge to the Authority given the already compounded impact of the significant government grant funding reductions and increased cost pressures it has incurred since 2010/2011. Although further budget efficiencies and IRMP actions are being developed under the proposed IRMP 2017/20 to meet the projected gap, it should be noted that a temporary use of reserves may be necessary in the medium term until permanent budget reductions are achieved. This practice has served the Authority well over previous financial years.

2.4 Key points to note which impact on Budget Planning for 2019/2020 and beyond are set out in the following sections of the report. However it is important to note that the Chancellors Autumn Budget may have further impacts upon the budget planning process. This will be kept under review with any significant matters affecting the Budget 2019/2020 being reported to members as appropriate.

3 National Economic Context to the 2019/2020 Budget

3.1 The government's aim is to achieve a balanced position on the national economy with no underlying deficit by the middle of the next decade. The March 2018 Spring Statement forecast that, as a percentage of GDP, debt would show a sustained decrease reducing from 85.5% of GDP in 2018/2019 (budget deficit of £37.1bn) before falling back to 77.9% of GDP in 2022/2023 (budget deficit of £21.4bn).

3.2 The UK's exit from the European Union may potentially have a significant impact on local government that cannot be factored in at this time and adds more uncertainty to the budget planning process.

3.3 On 2nd August 2018, the Bank of England (BoE) increased interest rates from 0.50% to 0.75%, the highest level since March 2009. However they emphasised that future Bank Rate increases would be gradual. The Lead Authority's treasury advisors do not think the Monetary Policy Committee (MPC) will increase the Bank Rate before the deadline for Brexit in March 2019. They predict the MPC is more likely to wait until August 2019, followed by increases in May and November 2020 reaching a level of 1.50%.

3.4 The BoE also revised its growth forecasts for the UK economy in the August 2018 Inflation Report, with latest predictions on growth now up to 1.5% (from 1.4%) in 2018 and up to 1.8% (from 1.7%) in 2019. CPI inflation increased to 2.5% in July 2018 (from 2.4% in June 2018) with the BoE projecting that inflation will reduce gradually to 2.2% in 2018 before reaching the target rate of 2.0% in 2021.

3.5 With Brexit negotiations taking place and potential geopolitical events outside the control of the UK government, economic and interest rate forecasting remains very difficult as there are many influences weighing on the UK economy. Forecasts are predicated on an assumption that sufficient progress is made, in respect of negotiations, to produce an agreement for Brexit that benefits both the EU and the UK. The economic outlook could be influenced significantly by the response of households, businesses and financial markets to developments related to the process of EU withdrawal.

3.6 In summary, there is consequently considerable uncertainty over external factors that could impact upon the Authority's Budget for 2019/2020 which the Authority has very little control over.

4 Government Core Funding

4.1 The Authority accepted the four year funding settlement offer made by Government which sets out the levels of Revenue Support Grant (RSG) that the Authority will receive up to 2019/2020. The offer is limited to the level of indicative funding provided through this funding source only and there is currently no detail published by Government beyond 2019/2020, which again adds another layer of uncertainty around the availability of resources into the medium term.

4.2 Based on the indicative budget allocations, Government funding is forecast to reduce overall by £0.548m in 2019/2020 compared to the previous year. Of this, Revenue Support Grant (forecast to be £8.796m), accounts for most of this reduction (i.e. £0.824m or -9%). Top up grant and the business rates multiplier are anticipated to increase in line with inflation using the lower measure of CPI. The Government's figures also assume growth in council tax (both in the tax base and the precept). These estimates, however, fail to recognise local circumstances and any adverse impacts of the introduction of Universal Credit across the region. This means that there is very limited flexibility in the funding available to the Authority that is not already included in the Government's Core Spending Power forecasts, unless Government review their referendum limits for the fire service and allow higher increases in Council Tax.

4.3 The government released a Local Government Finance Settlement 2019/2020 – Technical Consultation Paper in the summer asking Authorities for their views on a number of technical issues. The response to the relevant questions impacting upon the Authority are set out in detail in Appendix 1 for members' information. Our response highlights the need for additional resources from Government and more flexibility in setting Council Tax levels.

5 Local Income

5.1 Council Tax

The Localism Act provides for the provision of referendums to veto excessive council tax (precept) increases. This effectively places a limit on council tax increases and if authorities exceed the government limits, the public will be able to vote to agree or veto any increase considered ‘excessive’. For 2018/2019 a referendum requirement applied for proposed increases in Council Tax above 2.99% and government has indicated this will remain the case for 2019/2020.

The current Medium Term Financial Strategy has therefore assumed a 2.99% increase in its Council Tax precept for 2019/2020 to take account of these government assumptions. However, a decision on the application of this option will need to be made as part of the budget planning process, once all other funding factors are understood from the Finance Settlement. Should the Authority be granted flexibility around the level of precept increase, options will be considered to maximise income from this funding stream. Members will be consulted and decisions will be made as the budget is set.

The Local Council Tax Support Scheme was introduced from April 2013 and is in its sixth year of operation. The Authority’s Council Tax income could be affected by the individual schemes agreed by each of its district councils and therefore any proposed changes to the current schemes in operation will need to be assessed for any impact on Council Tax income for 2019/2020, along with any adverse impacts from the introduction of Universal Credit across the region.

5.2 Business Rates

Under the current Business Rates Retention Scheme, the Authority is allocated locally 2% of the increased business rates income arising from growth in the Local Business Rates base from its constituent authorities (however equally it shares the risk of any under achievement of income targets).

Inherent within the scheme is growth arising from annual inflationary increases to Business Rates. However, there is continuing uncertainty, specifically around appeals and avoidance tactics, which can significantly impact on the level of income collected each year. The position will be kept under review and changes to Business Rates income will be reflected in the Budget Planning Framework as appropriate.

5.3 Reserves and Balances

The Local Government Finance Act 1992 requires local authorities to have regard to the level of reserves needed for meeting estimated future expenditure when calculating its budget requirement each year.

In accordance with the approach adopted to date, all earmarked reserves will be revisited and fully reviewed as part of the budget process to ensure they still accord with the Authority’s priorities and overall funding position.

A separate review of reserves will be reported to members in March once the MTFS and Budget for 2019/2020 have been approved.

6 Other Funding Issues

6.1 Changes to Retained Business Rates

At this stage the Government's plans for Business Rates retention remain unclear. The Government had proposed to introduce 75% retention of business rates by 2019/2020 but current timescales suggest a broad outline of the new system will be published by Winter 2018, with indicative figures not available until Summer 2019.

In parallel, the Government are reviewing the needs based element of the funding formula and this change could be implemented without the need for primary legislation. Both the Ministry for Housing, Communities and Local Government (MHCLG) and Local Government Association continue to discuss and work on a 'fairer funding' regime.

This uncertainty makes financial planning beyond 2019/2020 extremely difficult. In the absence of detailed information in relation to the impact of the fair funding review, 75% retained business rates and the Comprehensive Spending Review, it is assumed for budget planning purposes at this stage that the Government will take action to ensure a 'status quo' impact on the funding position for each authority through the top ups and tariff system, to ensure no detrimental impact on each authority's overall funding position in the initial year of 2020/2021.

6.2 Brexit Arrangements

The Government has recently started to issue EU Exit Technical Notices covering what may happen in the event of a 'No deal Brexit' to regulations or programmes which are currently regulated or funded with the EU. These notices and the progress on talks regarding the future relationship between Britain and the EU are being kept under close review so as to understand any potential impact which may arise on the Authority's Revenue Budget and Capital Programme and longer term resources.

7 Spending Pressures and Commitments

In addition to funding changes, the Authority must also plan for a range of spending pressures and commitments that are not funded by Government. It is proposed to take into account the following spending commitments in the Budget Planning Framework for 2019/2020, noting that in a number of cases specific cost details cannot be finalised at this stage and will be subject to further review and refinement throughout the budget setting process:

7.1 Pay and Pensions

7.1.1 Pay

- Non Uniformed
  Trade unions accepted a two year pay offer for Local Government covering the period to 31st March 2020. Provision for the impact of the agreed 2% pay award for 2019/2020 has been factored into the budget planning.

- Uniformed
  A provision of 2% remains factored into the budget for uniformed staff following agreement of this, on account, while negotiations continue.

  The position with regard to the pay award and future year assumptions will be kept under review throughout the budget process.

7.1.2 National Living Wage

The government implemented the national living wage of £7.20 with effect from April 2016. This has increased annually and latest forecasts from the Office of Budget Responsibility suggest an increase to £8.20 in 2019, rising to £8.57 by April 2020. This represents an additional cost pressure for the Authority both through own staffing costs and external contract suppliers passing the costs on through increased contract prices. Provision has been factored into the Budget Planning Framework.

7.1.3 Pensions

Local Government Pension Scheme
The Triennial Actuarial review of the Local Government Pension Scheme was concluded in March 2017. The outcome of the review is reflected in the budget planning. The next Actuarial review is scheduled to impact from 2020/2021 and prudent provision is included within the budget for the potential impact.

Firefighters Pension Scheme
Government changes to the scheme came in to force from 1st April 2015 with the addition of the new 2015 scheme and Modified Scheme and changes to both employer and employee contribution rates across the firefighter pension schemes. The financial implications have been built in to the base budget and will be kept under review.

An actuarial valuation of the Firefighters Pension Scheme is undertaken every four years, with the next one scheduled to impact from 2019/2020. The output of this valuation will be an updated employer contribution rate expected to apply from April 2019 to March 2023. It is estimated that the current average employer contribution rate of 17.6% will be increased to 30.2%. This will be a significant additional cost pressure for the Authority from 2019/2020. Prudent provision is already included within the MTFS of £0.5m based upon information provided by the Government in their Spring 2016 Budget. However latest indications suggest that if the full costs are passed on to the employer, this could cost the Authority £2.6m because of further changes made by the Government to those set out in 2016, which will significantly increase the costs to all Fire and Rescue Authorities. Because the full implications of this are not yet known, this is not included within the MTFS at this stage.

7.1.4 Apprenticeship Levy

The Apprenticeship Levy, introduced in April 2017 for large employers (over 250 employees) was reflected in the base budget from 2017/2018. For Tyne and Wear Fire and Rescue Authority the cost in 2019/2020 is expected to be in the region of £0.125m. The Authority has acquired a managed apprenticeship service and is progressing its options on how it can best utilise the Levy funds available to the Authority. The outcomes will be reflected in the 2019/2020 budget as plans are developed with the providers Learning Curve.

7.1.5 Energy Prices

Energy and vehicle fuel prices continue to be volatile. It is therefore proposed that prudent provision be included for continued annual increases in charges for gas, electricity and vehicle fuel for the medium term. However, it is also important to note that increases continue to be lower than anticipated because of the Authority's proactive approach and actions it has taken in respect of developing and then implementing its carbon management policy.

7.1.6 Capital Financing

No prudential borrowing has been included within the medium term financial position at this stage, but the position will be continuously reviewed to ensure that the future use of resources reflects best value and can be adapted to enable strategic priorities of the Authority to proceed in the future as required.
However the current position of using reserves to fund the Authority's Capital Programme in the longer term is not sustainable and borrowing will need to be considered as appropriate.

8 4 Year Efficiency Plan

8.1 The Efficiency Plan 2016/2017 to 2019/2020, which was a requirement by Government for the Authority being able to accept the Four Year Grant Settlement, was agreed and published in September 2016. The plan details the Authority's approach to the delivery of savings necessary to address the reductions in funding and spending pressures it faces over the four year period.

8.2 The Efficiency Plan originally identified savings totalling £8.248m to be achieved over the four year period, based on the Authority's Medium Term Financial Strategy (MTFS) 2016/2017 to 2019/2020 which was reported to members in February 2016. However, the actual budget gap has continued to widen over the 4 year period, which the Authority will still need to address. This position is recognised in the revised and updated MTFS published annually by the Authority.

8.3 The table overleaf shows, in summary, the total planned savings each year and how the Authority proposed to achieve these through a combination of Revenue Budget Efficiencies and planned actions from the Authority's Integrated Risk Management Plan (IRMP), a fully costed Plan which sets out separate, much wider major reviews of service areas to achieve savings.

	4 Year Plan	Updated Plan	Actuals
	£000	£000	£000
2016/17 – efficiencies	1,323	1,323	1,323
IRMP actions	1,184	1,184	1,184
2017/18 – efficiencies	1,394	1,394	1,441
IRMP actions*	1,773	2,338	2,267
2018/19 – efficiencies	4	4	948
IRMP actions*	1,081	516	923
2019/20 – efficiencies	0	0	130
IRMP actions	1,489	1,489	106
Total	8,248	8,248	8,322

*The updated plan reflects the fact that the Authority implemented the Organisational Management Review in full from 2017/18 saving £1.690m. In the original plan this was expected to straddle 2017/18 and 2018/19.

8.4 It is pleasing to report that the Authority has found savings of £8.086m by the end of 2018/2019, a total of £1.327m more than that set out in the Efficiency Plan and has now exceeded its planned 4 Year Efficiency Plan savings total by £74k. This is testament to the Authority, the hard work of its staff and members in making difficult decisions to save money and its excellent track record in achieving both IRMP and Budget efficiencies. However the Authority faces not only further grant funding reductions, but also continued spending pressures, such as significant inflationary cost increases, pay awards and revaluation of the firefighters' pension scheme, which has meant that the Revenue Budget gap has continued to widen from that estimated in 2016/2017 when the 4 Year Settlement was implemented. This means that the Authority is still currently £2.316m short of balancing its Revenue Budget in 2019/20 (MTFS) despite exceeding its overall savings objective target in its 4 Year Efficiency Plan. Any additional savings in addition to those reported in the Table above will however help to reduce the budget gap of £3.7m identified at the end of 2021/2022.

8.5 It should be noted that the Authority has already made very difficult budget cost reductions that have impacted upon all areas of the service. Front line services have been affected, both in terms of reducing firefighter numbers and changes to the response model in operation. The base budget has been reduced significantly since 2010/2011 by 19.7% and the Revenue Budget gap identified in the MTFS up until 2021/2022 of £3.690m will become much more challenging for the Authority to address as a result.

8.6 Going forward, the Authority is progressing its IRMP 2017/2020 actions, updates of which are included on today's agenda. These reviews cover Response, Collaboration and Ways of Working and once approved, the savings can then be factored into the Medium Term Financial Strategy. In the medium term it is recognised that temporary use of reserves may still be needed until these actions can be implemented and permanent budget reductions achieved.

9 Fire Injury Pensions

9.1 The Authority, as members will know, agreed a schedule to repay over claimed pension top up grant. An initial payment of £1.892m was made in 2017/2018 and the remaining £8.639m will be repaid by equal instalments of £0.500m from 2018/2019 to 2034/2035, with a final amount of £0.139m payable in 2035/2036. Consequently the £0.500m annual liability has been included in the revenue base budget, so forms part of the 2019/2020 Revenue Budget. This will continue to be monitored to ensure it remains affordable.

10 Summary Resources, Pressures and Commitments Position

10.1 The total reduction in resources and spending pressures represents the estimated gross funding gap. However, at this stage there remains a number of significant uncertainties:

- The Chancellor's Autumn Budget Statement;
- The Local Government Finance Settlement for 2019/2020, which will not be available until December;
- Grant announcements in relation to Fire Revenue Grants;
- The Government plans in relation to Fair Funding, Business Rates and the departmental spending review all impacting on 2020/2021;
- The general economic position and public sector finances including any potential impact of Brexit negotiations;
- Impact of further roll out of Universal Credits on Council Tax income;
- The Districts' Collection Fund positions for both Council Tax and Business Rates;
- Confirmation and update on IRMP savings assumptions
- Any additional pension contributions costs associated with the actuarial valuation of the firefighters pension scheme; and
- Additional budget pressures which may arise throughout the remainder of the budget process.

11 Proposed Budget Planning Framework for 2019/2020

11.1 It is proposed the budget planning framework as set out below is adopted:

- Budget planning to be based on the high level position outlined at paragraph 2 and updated in light of the Chancellor's Autumn Budget 2018 and the Local Government Finance Settlement expected in December 2018;
- Provision for spending commitments to be included at this stage on the basis set out at section 7 and kept under review;
- Budgets to be prepared on the basis that all spending pressures not specifically identified above as commitments be accommodated within existing budgets;
- The position regarding the Council Tax Precept increase will need to be kept under review and if there is a relaxation of the referendum limit, any increased flexibility will need to be fully considered by members as part of the budget setting cycle, with confirmation of these proposals being sought as soon as practicably possible; and
- Commitments against General Fund Balances and Earmarked Rreserves to be reviewed and updated as necessary throughout the budget process.

12 Risk Management Implications

12.1 Risk implications have been considered in drafting the necessary guidance which is an essential early part of the Authority's robust revenue budget planning arrangements. The approach is reasonable and there are no real concerns or risks that have not been included within the report at this stage.

13 Financial Implications

13.1 The Budget Planning Framework provides the necessary guidance and information on the key financial aspects that will need to be considered by the Authority in drafting the 2019/2020 Revenue Budget to be approved by members in February 2019. At this early stage, however, there are no direct financial implications apart from those areas contained within the report.

14 Health and Safety Implications

14.1 There are no Health and safety implications from this report at this stage.

15 Equality and Fairness Implications

15.1 There are no equality and fairness implications in respect of this report.

16. Recommendations

16.1 Members are recommended:

a. To note the contents of the report and the estimated funding gap based on the most up to date information;
b. To agree the proposed Budget Planning Framework summarised at Section 11 of the report which will guide the preparation of the Revenue Budget for 2019/2020; and
c. To note the updated current Medium Term Financial Strategy and that the full Medium Term Financial Strategy 2019/2020 to 2022/2023 will be presented to Authority in February 2019.