

## MEDIUM TERM FINANCIAL STRATEGY 2020/21-2022/23

### JOINT REPORT OF THE CHIEF FIRE OFFICER AND TREASURER



**For Approval**

#### 1. PURPOSE OF REPORT

- 1.1 To enable Members to consider and approve the recommendations referred from the Executive Committee in relation to medium term financial strategy.

#### 2. RECOMMENDATIONS

- 2.1 The following recommendations have been referred from the Executive Committee:
- (i) Members note the report and that further updates will be provided later in the year to enable Members to consider the final recommendations to be referred by the Executive Committee to manage the forecast Collection Fund deficit and set the 2021/22 budget and Council Tax level.
  - (ii) Approve the proposals to include budget provision for increased Fire Protection Capacity in the 2021/22 budget, noting this slightly increases the total forecast deficit for 2021/22 and 2022/23 from £446,000 to £547,000.

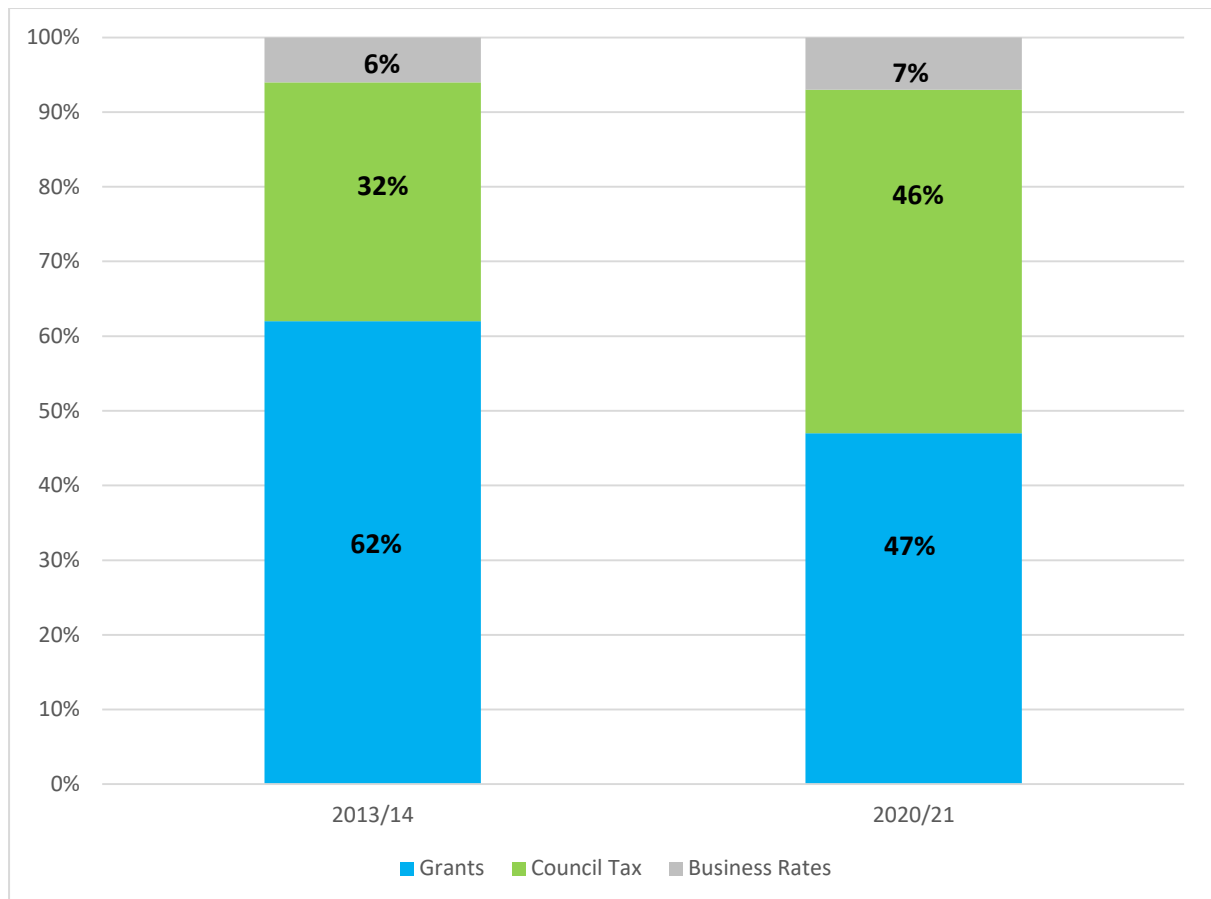
#### 3. BACKGROUND

- 3.1 To provide context to the Authority's future financial challenges Members are reminded that the Authority has previously managed nine consecutive years (2011/12 to 2019/20) of reductions in Government funding and this has resulted in the following changes:
- **36% reduction** in the number of **whole time firefighter posts** from 518 in 2010/11 to 330 in 2019/20.
  - **33% increase** in the number of **retained duty system firefighter posts** from 72 in 2010/11 to 96 in 2019/20.
  - **38% reduction** in the number of **fire control posts** from 26 in 2010/11 to 16 in 2019/20.
  - **19% reduction** in the number of **non-uniformed support posts** from 129.21 in 2010/11 to 105.15 in 2019/20.
  - **30% reduction** in number of Elected Members from 23 to 16 – effective from June 2016.

3.2 There has also been a significant shift in funding between 2013/14 (the year the current funding system was implemented) and 2020/21 as over this period:

- Government funding has fallen from **62%** of total funding to **47%**; and
- Council Tax has increased from **32%** of total funding to **46%**

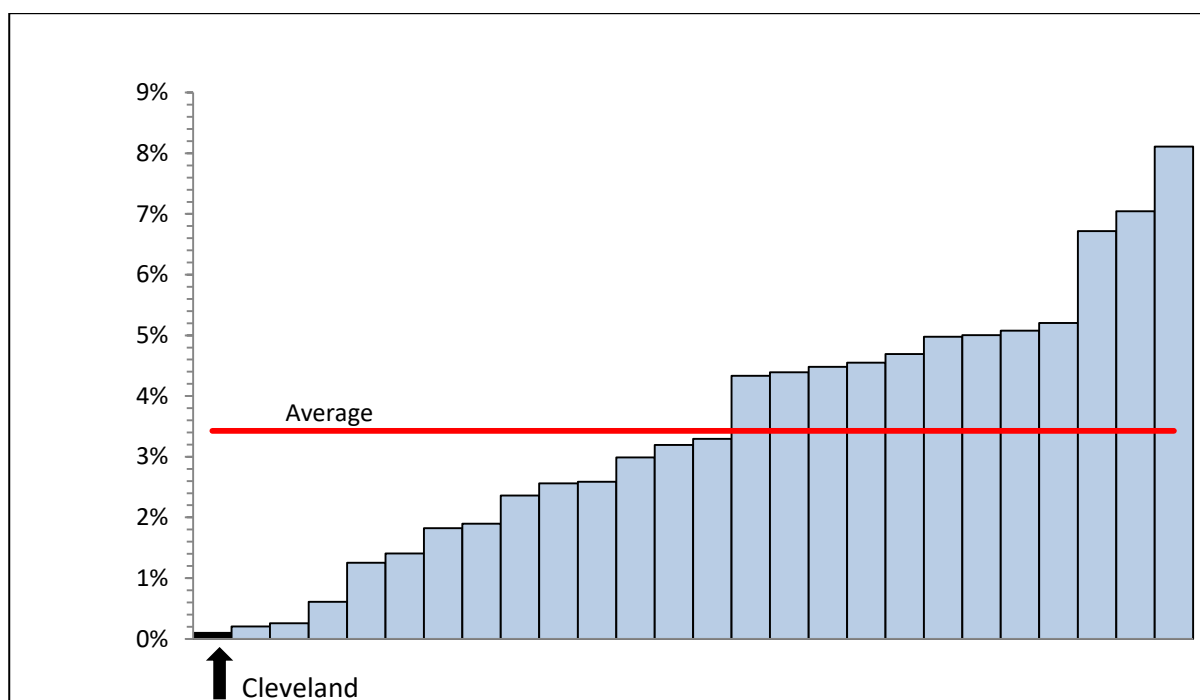
Funding Changes 2013/14 to 2020/21



3.3 The changes in funding, referred to by the Government as Spending Power, have varied significantly for Fire and Rescue Authorities (FRAs). FRAs, which includes Cleveland, with a low Council Tax base (i.e. high proportion of properties in Council Tax Bands A and B) have had less ability to offset Government grant cuts with increases in Council Tax income as these increases raise less additional income. This position was exacerbated by the fact that all FRAs have faced the same pay and inflation pressures.

3.4 Over the period 2015/16 to 2020/21 there has been a significant divergence in cumulative Spending Power increases for FRAs. This position is highlighted in the table below, which shows this difference was 8.0% (i.e. highest increase 8.1% less lowest increase 0.1% - which is Cleveland FRA).

Percentage Changes in Spending Power from 2015/16 to 2020/21



- 3.5 This situation will not change until the current funding system changes and the Government begins to increase grant funding to partly meet national pay award pressures and inflation. Without future annual increases in Government grant funding Council Tax increases will not be sufficient to cover expenditure pressures and this will mean further services cuts will be unavoidable.

#### **4. NATIONAL ISSUES**

- 4.1 Since the budget was approved in February the issues detailed in the following paragraphs have arisen and will impact on the financial position of the Authority.

##### **4.2 Pay Awards**

In July 2020 the Government accepted the Pay Review Bodies recommendations for various sectors – Teachers 3.1%, Police and Prison Officers 2.5%, and Armed Forces 2%. Separately a 2.75% has been agreed for Local Government employees, which includes non uniformed staff employed by FRS.

As part of the announcement of the 2020 Spending Review the Chancellor indicated “that after one-off above inflation pay awards for 2020/21 for many public sector workers that we must exercise restraint in future public sector pay awards”.

The Government will not be providing any additional funding for the 2020 pay increases. Therefore, if these increases exceed an individual organisations planning assumption they will need to manage the actual national pay awards within their overall resources.

The Government's decision not to provide additional funding for these increases is a clear indication that other parts of the public sector will have to fund 2020 pay awards from within existing resources, which includes the Fire and Rescue Service.

On 4 September the National Joint Council wrote to notify FRS that a 2% increase in pay rates has been agreed for Fire Fighters.

#### 4.3 National Funding Reforms

The Government has announced that the Fair Funding Review and proposed increase in Business Rates Retention from 50% to 75% will be delayed until 2022/23. These changes had originally been proposed to be implemented from April 2020. This further delay and the 2020 Spending Review makes financial planning extremely challenging as there is currently no national information to assess the potential local impact. Details will be reported as they become available.

#### 4.4 Spending Review 2020

On 21<sup>st</sup> July 2020 the Chancellor announced that a Spending Review will be completed and set a deadline of 24<sup>th</sup> September for submitting representation. When launching the 2020 Spending Review the Chancellor said:

- 'it is clear there will be "tough choices" in other areas of spending at the review, and departments have been asked to identify opportunities to reprioritise and deliver savings'.

The above statement reflects the large amounts already promised by the Government for priority areas like the NHS, schools and police. The Chancellor's emphasis on the need for 'tough choices' means another round of budget cuts for other departments and areas of public spending is a potential possibility.

The Chief Fire Officer and Treasurer agreed a submission with the Chair based on the following key principles:

- The Spending Review needs to provide sufficient funding in 2021/22 to 2023/24 to provide the same increase in Spending Power for all Fire and Rescue Services (FRS) in recognition that all FRS will face the same pay pressures from national pay awards.
- The Spending Review should continue to provide a specific grant for the increased pension costs to avoid FRS having to cut services if this funding does not continue;
- The Spending Review should provide funding to fully address Collection Fund deficits arising from the impact of Covid-19 as these issues are outside the control of FRS;

- Remove FRS from the Business Retention system and replace this income with additional grant funding. Whilst this income only makes up a small proportion of overall funding, it exposes FRS to significant potential financial risks. This proposals would put FRS on the same basis as the Police Service which does not receive a share of Business Rates income. Neither organisations have a direct role in securing economic development, which is a council responsibility, although they make a significant contribution to community wellbeing and safety.

A copy of the Spending Review submission from the Local Government Association and National Fire Chiefs Council is attached at **Appendix A** and the Authority's submission is attached at **Appendix B**.

## **5. 2020/21 BUDGET POSITION**

- 5.1 In response to continued uncertainty regarding Government funding for 2021/22 and future years the Chief Fire Officer has continued to manage the current year's budget extremely carefully. A managed underspend of £500,000 is currently forecast and includes the impact of staff turnover. It is recommended that this amount is earmarked to support the Budget Support Fund which will need to be used to address the 2020/21 Collection Fund deficit and the 2021/22 budget deficit, as detailed later in the report.

## **6. FINANCIAL IMPACT OF COVID-19 ON SERVICE EXPENDITURE**

- 6.1 The Authority has received grant funding of £587,000 to meet the additional costs of responding to the Covid-19 pandemic. These resources have been used to cover PPE costs and overtime costs. It is anticipated that this funding should be sufficient to meet the expenditure impact of Covid-19, provided there is not a second outbreak. As detailed in the next section this funding will not cover the Collection Fund deficit arising from the economic impact of the pandemic.

## **7. FINANCIAL IMPACT OF COVID-19 ON RESOURCES**

- 7.1 The amount of money the Authority will receive in 2020/21 for the Council Tax precept and share of Business Rates income is guaranteed at the level forecast when the budget was set. This income is paid from the Collection Funds managed by the four constituent councils.
- 7.2 However, there will always be changes to these forecasts during the year and these changes will be accounted for within the Collection Fund balance at the end of the financial year. This balance can either be:
- **A surplus** - where actual income is greater than forecast, which for example could reflect higher housing completions than forecast, an increase in business ratepayers, or a reduction in the number of households eligible for Local Council Tax Support; Or
  - **A deficit** - where actual income is less than forecast, which for example could reflect lower housing completions than forecast, a decrease in business ratepayers, or an increase households eligible for Local Council Tax Support.

- 7.3 Collection Fund surpluses/deficits are shared in proportion to the precepts set by councils, fire and police (Council Tax only as police do not share Business Rate income). Current regulations require Collection Fund balances to be accounted for a year in arrears.
- 7.4 In normal circumstances Council Tax Collection fund balances are generally not significant, for example when setting the 2020/21 budget the Authority received a 2019/20 surplus of £52,000 - to provide context to this figure the 2019/20 Council Tax precept was £11.868m. This is also generally the case for Business Rates, for example the 2019/20 deficit was £9,000 – to provide context the 2019/20 Business Rates income was £1.833m.
- 7.5 Covid-19 will have an unprecedented impact on the 2020/21 Collection Funds and there will be significant deficits. This position has been recognised by the Government as they have indicated that 2020/21 Collection Fund deficits can be repaid over three financial years – i.e. 2021/22, 2022/23 and 2023/24.
- 7.6 Whilst the ability to spread 2020/21 Collection funds will be helpful from a cash-flow perspective the Government's current proposal still means the Authority will have to fund this loss of income from existing resources. It is still hoped that the Government will recognise the impact of Collection Fund deficits and provide additional grant funding to support these unforeseen income reductions.
- 7.7 The forecast 2020/21 Council Tax Collection Fund deficit reflects the impact of Covid-19 on two factors:

- **An increase in households eligible for Local Council Tax Support (LCTS)**

Responsibility for LCTS transferred to local authorities in 2013/14 and changes in households eligible for LCTS now feed through to the Council Tax base. If there is a decrease in households eligible for LCTS there is an increase in the Council Tax base and income. If there is an increase in households eligible for LCTS there is a reduction in the Council Tax base and income. This is the position now facing the Authority. Before 2013/14 the costs of any increase in households eligible for Council Tax support fell fully on the Government.

Since 2013/14 economic conditions had been broadly positive and all four constituent councils had seen a reduction in households eligible for LCTS to the start of 2020/21.

Covid has caused the first economic shock since LCTS was introduced and as unemployment increases and / or employers reduce peoples working hours there will be an increase in households eligible for LCTS. This means the number of households paying 100% Council Tax will reduce. Households eligible for LCTS pay reduced Council Tax of between 12% and 20% depending on where they live.

The four constituent authorities have already seen an increase in the pre-Covid level of households eligible for LCTS support. It is expected the withdrawal of the furloughing scheme will lead to a further increase as unemployment increases and / or employees working hours are reduced.

- **A reduction in forecast housing completion**

The number of housing completions is forecast to be lower than forecast owing to the initial shutdown of construction sites and subsequent reduction in the number of new houses completed and occupied.

- 7.8 Over the course of 2020/21 it is currently anticipated that the above factors may result in a Council Tax Collection Fund deficit of between **3% (£370,000)** and **5% (£615,000)** of forecast Council Tax income. In accordance with national regulations this income reduction will not impact in 2020/21, but will need to be addressed when the budgets for 2021/22 and future years are developed. This reduction in income will take a number of years to recover to the pre-Covid level and a strategy for managing this position is detailed in paragraph 7.10.
- 7.9 The level of Business Rates income will be lower than forecast and this may result in a Business Rates Collection Fund deficit. This is a less significant financial issue for the Authority as Business Rates makes up only **£1.868m** of forecast income. In addition, the Government is providing significant Business Rates relief for defined sectors and the Authority will receive a Section 31 grant to replace this income.

#### **7.10 Strategy for managing forecast Income Reductions**

- 7.11 It is anticipated that the above income reductions will be temporary. However, it is difficult to assess when income levels will recover to the pre Covid levels previously forecast in the MTFS. There is also uncertainty regarding whether the Government support will be limited to the ability to repay Collection Fund deficits over three years, or whether the 2020 Spending Review will provide additional grant funding.
- 7.12 The major uncertainty relates to the increase in LCTS eligible households and how quickly this increase then reverses to pre-Covid levels. For planning purposes two scenarios have been modelled:
- Best case - the increase in LCTS eligible households reduces Council Tax income by 3%
  - Worst case - the increase in LCTS eligible households reduces Council Tax income by 5%. Based on current information this is the most likely position.
- 7.13 For both scenarios it is anticipated that recovery will take three years and on this basis the following income shortfalls are forecast:

Forecast income shortfall 2020/21 to 2022/23

	Best Case – Income reduction £'000	Worst Case – Income reduction £'000
2020/21 Council Tax income reduction	370	615
2020/21 Business Rates income reduction	50	50
<b>Sub Total 2020/21 Forecast Income reduction</b>	<b>420</b>	<b>665</b>
2021/22 Council Tax income reduction	185	307
2021/22 Business Rates income reduction	25	25
<b>Sub Total 2021/22 Forecast Income reduction</b>	<b>210</b>	<b>332</b>
2022/23 Council Tax income reduction	90	153
2022/23 Business Rates income reduction	25	25
<b>Sub Total 2022/23 Forecast Income reduction</b>	<b>115</b>	<b>178</b>
<b>Total Forecast Income reduction</b>	<b>745</b>	<b>1,175</b>

- 7.14 Against this uncertain background and the temporary nature of the forecast income shortfalls it is recommended that these shortfalls are funded from the Budget Support Fund. This strategy will avoid these issues impacting on the main MTFs strategy. This will provide time to assess how quickly income returns to pre-Covid levels and avoid the need for cuts in services, which may not be necessary in the medium term if income returns to the pre-Covid level. The impact of this strategy on the Budget Support Fund is detailed later in the report.

## **8. 2021/22 BUDGET AND 2022/23 FINANCIAL OUTLOOK**

- 8.1 The timing of the Spending Review means the provisional 2021/22 Local Government Finance Settlement is unlikely to be issued until late December, which makes financial planning for 2021/22 difficult. Delays of major reforms to the Local Government Funding system until 2022/23 also make financial planning difficult.
- 8.2 For planning purposes it is assumed that for 2021/22 and 2022/23 the Government will retain grant funding at the same level as 2020/21 – i.e. **£12.758m**. This cannot be guaranteed as the Government's Spending Review may result in cuts to this funding.
- 8.3 For planning purposes it has also been assumed that:
- The Government will maintain 2021/22 and 2022/23 Council Tax Referendum Limits at 2% and Members will approve these increases to protect the Authorities recurring income. In 2021/22 a 2% Council Tax increase will provide additional recurring income of approximately £240,000 and a further £240,000 in 2022/23;
  - The Government will not provide additional funding for public sector pay awards and any agreed national increases will have to be funded from available recurring resources;
  - Inflation will remain low;

- Collection Fund Deficits in 2021/22 will be funded as detailed in the previous section;
- The economic impact of Covid-19 will reduce forecast housing growth over the period 2020/21 to 2022/23;

8.4 Provision has also been included within the 2021/22 budget forecast for increased Fire Protection capacity. On the basis of these forecasts and continuation of the Fire Pension Grant the forecast total deficit for 2021/22 and 2022/23 has increased from £446,000 to £547,000, as follows:

Forecast Budget deficit **WITH** Fire Pensions Grant Sustained

	2021/22 £'000	2022/23 £'000	Total £'000
Forecast reported February	375	172	547

8.5 **Fire Pension Grant**

8.6 The position regarding the Fire Pension Grant remains uncertain and it is anticipated this issue will now be addressed as part of the 2020 Spending Review. This is a significant issue as this grant is **£1.408m** in the current year. As this funding was specifically provided to meet additional national costs of providing Firefighters pensions the withdrawal of this funding would have a detrimental impact on the Authority's financial position. To put this figure into context it equates to **11%** of Core Government grant funding allocated to the Authority, or to put it another way it is the funding needed for **28** Firefighters posts.

8.7 If the Fire Pension Grant is phased out over three years commencing 2021/22 this would increase the 2021/22 and 2022/23 deficits and also defer additional cuts of £0.468m per year to 2023/24, as summarised below:

Forecast Budget deficit **WITHOUT** Fire Pensions Grant Sustained

	2021/22 £'000	2022/23 £'000	Total £'000
Forecast if Pension Grant continues	375	172	547
Add - Phasing out of Pension Grant commencing 2022/23	470	470	940
<b>Revised Deficit WITHOUT Fire Pension Grant Sustained</b>	<b>845</b>	<b>642</b>	<b>1,487</b>

8.8 The deficits for the above two scenarios will increase if:

- the 2020 Government Spending Review results in a further period of austerity as each 1% Government Grant cut would require the Authority to make additional budget cuts of **£127,000**.
- National pay awards exceed the budget provision and are not fully funded with additional Government grant as each additional 1% increase for Firefighters equates to approximately **£200,000**.

**8.9 Strategy for managing 2021/22 and 2022/23 forecast budget deficit**

- 8.10 In view of the significant uncertainty regarding Government funding for 2021/22 and 2022/23 it would potentially be premature to plan to make cuts for 2021/22. Therefore, to address the 2021/22 budget deficit it would be appropriate to use the Budget Support Fund. This strategy will reduce the uncommitted Budget Support Fund, although the reduced value of this reserve will still provide financial flexibility to help manage financial risks beyond 2021/22 as detailed in section 9.
- 8.11 In adopting this strategy Members need to recognise that this is not a permanent solution as it defers a budget deficit until 2022/23. Therefore, it still remains appropriate for the Chief Fire Officer to develop a contingency savings plan to address the forecast 2022/23 deficit of between **£0.547m and £1.487m**. This approach will provide an appropriate lead time if it is necessary to implement budget cuts in 2022/23.
- 8.12 The higher deficit figure reflects the potential withdrawal of the existing Pension Grant and if this situation arises it may be appropriate to use some of the uncommitted Budget Support Fund in 2022/23 to again support the phasing of further budget cuts. However, this decision will need to be made in the context of the financial outlook for 2022/23 to 2024/25, as it is hoped that a multi-year Government Grant Settlement will be provided for these years.

**9. RESERVES**

- 9.1 A comprehensive review of reserves will be completed and reported to a future meeting. At 31<sup>st</sup> March 2020 the Authority had total reserves of £9.755m (£10.837m at 31<sup>st</sup> March) as detailed in **Appendix C**.
- 9.2 In terms of the resources available to support the budget and the financial impact of Covid-19 the Authority has two reserves – the Budget Support Fund and Council Tax Collection Fund Deficit Reserve:
- 9.3 The Budget Support Fund reserve is earmarked to manage the significant financial uncertainties facing the Authority from planned national funding changes, which as detailed earlier in the report have been delayed. The Council Tax Collection Fund Deficit Reserve is earmarked to help mitigate the impact of Covid-19 on Council Tax income.
- 9.4 The availability of these reserves helps the Authority manage the impact of Covid-19 and support the 2021/22 budget. Proposals recommended in this report will reduce the level of these reserve from **£4.933m** to between **£3.584** and **£4.054m** as summarised below. The reduced level of this reserve will still provide an appropriate level of financial flexibility to meet other unforeseen issues and to temporarily support the budget in 2021/22 and 2022/23 if Government funding is reduced.

Summary of reduction in Budget Support Fund  
and Collection Fund Deficit Reserve

	Best case – Pension Grant continues in 2021/22 £'m	Worst case – Pension Grant phased out commencing 2021/22 £'m
Budget Support Fund 31.03.20)	4.533	4.533
Collection Fund Deficit Reserve (31.03.20)	0.400	0.400
<b>Sub Total (31.03.20)</b>	<b>4.933</b>	<b>4.933</b>
Add - Approved 2020/21 contribution – funded from final increase in resources	0.171	0.171
Add – Forecast 2020/21 contribution towards Collection fund deficit	0.500	0.500
Less – Forecast Collection Fund Deficit	(1.175)	(1.175)
Less - Forecast support of 2021/22 Budget	(0.375)	(0.375)
Less – Additional potential support of 2021/22 Budget if Pension Grant phased out	0.000	(0.470)
Forecast Uncommitted Balance	<b>4.054</b>	<b>3.584</b>

## 10. CONCLUSION

- 10.1 Prior to 2020/21 the Authority had managed nine years of austerity and cuts in Government grant funding. As the majority of the budget is spent on front line services the Authority has made significant changes, including reductions in the number of whole time firefighter posts, as detailed in section 3.
- 10.2 The financial environment facing local government and FRAs is probably the most uncertain the sector has ever faced. The list of uncertainties is a significant challenge to budget planning and the key issues, in no particularly order are:
- the outcome of the 2020 Spending Review;
  - the impact of delayed major reforms of the funding system until 2022/23;
  - the impact on the collection fund of the pandemic in the current year;
  - the impact on both the council tax base and business rates base of the economic down turn;
  - the overall level of grant funding in the settlement for 2021/22;
  - the trigger level for the 2021/22 council tax referendum limits;
  - the possibility of a second Covid-19 wave locally or nationally; and
  - the size and shape of the economic recovery, both nationally and locally.

- 10.3 The Authority has previously set aside one off resources in the Budget Support Fund and Collection Fund Deficit reserves to manage financial risks and uncertainty. Therefore, the recommended strategy is to use some of these reserves to support the 2021/22 budget and the reductions in Council Tax and Business Rates income arising from the economic impact of Covid.
- 10.4 This strategy is an appropriate way of managing financial uncertainty and income reductions, which are outside the Authority's control. However, Members need to recognise that using reserves is not sustainable and the strategy is designed to provide a longer lead time to manage the budget position. It therefore remains appropriate for the Chief Fire Officer to develop a contingency plan to address a current forecast deficit between **£0.547m and £1.487m** for 2022/23.

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