CHESHIRE FIRE AUTHORITY

MEETING OF: CHESHIRE FIRE AUTHORITY
DATE: 6TH DECEMBER 2017
REPORT OF: HEAD OF FINANCE
AUTHOR: WENDY BEBBINGTON

SUBJECT: CAPITAL, RESERVES AND BORROWING

Purpose of Report

1. To outline the Authority's capital position; to confirm the Authority's reserves position; to explain the current borrowing context; and to seek authority to borrow.

Recommended: That Members

[1] Approve the use of borrowing to fund the training centre project (and associated works) at Sadler Road to preserve reserves for other matters requiring capital expenditure.

[2] Authorise the Head of Finance in consultation with the Chief Fire Officer and Chief Executive to borrow up to £9m from the Public Works Loan Board when the time is right and using the best available option at that time.

Background

<u>CAPITAL</u>

<u>Capital Grant</u>

2. The Authority, like other public sector bodies used to receive an annual capital grant from the Government. Since 2014 the Authority has not received an annual capital grant. It seems extremely unlikely that such a grant will be reintroduced under the current financial constraints.

3. The Authority has been successful in securing specific capital grant which helped to fund two of the new fire stations and the safety centre. Unfortunately, there have been no opportunities to bid for specific capital grant in recent years. There is no indication that such opportunities will arise again under the current financial constraints.

4. It is considered prudent to plan on the basis that there will be no form of capital grant from the Government in future.

Capital Expenditure

5. Since 2014 the Authority has invested significant sums in buildings, fire appliances and operational equipment. This capital expenditure has been funded from specific capital grants and reserves. This has helped to mask the underlying requirement for regular capital expenditure, e.g. replacement of fire appliances, which in the past would have been funded from annual capital grant from the Government. This regular capital expenditure is obviously necessary to ensure that fire appliances and operational equipment can be replaced at appropriate intervals. It is estimated that the current level of regular capital expenditure that is required (for fire appliances and operational equipment – with no allowance for IT replacement costs) is circa £1.5m to £2m at current costs.

6. Once reserves are exhausted the Authority will need to borrow in order to fund this regular capital expenditure. The cost of borrowing will need to be funded from revenue, which means that savings will need to be found in order to fund this regular capital expenditure.

Capital Investment

7. The Authority has allocated £9m for the training centre project (and associated works) at Sadler Road.

8. The Authority's regular capital expenditure over the next four years is expected to be in the region of £7m.

9. The Authority has aspirations (or needs) to replace two or three of its existing fire stations, which will cost between £3.5m and £5.5m at current costs.

10. The Authority will also need to invest in its other fire stations (and its houses). Whilst it is difficult to offer a worthwhile figure for this it is clear that it will be a considerable sum to be spent over the next four or five years.

11. It is clear that a significant proportion of this capital investment will need to be funded by borrowing.

RESERVES

12. At the 1 April 2017, the Authority held £28.1m in reserves as shown in the table below.

	31-Mar-17 £000	31-Mar-18 £000	31-Mar-19 £000	31-Mar-20 £000	31-Mar-21 £000	31-Mar-22 £000
IRMP related	(10,216)	(8,221)	(3,489)	682	1,282	1,282
Capital receipts	(340)	(372)	(342)	(312)	(281)	(250)
Capital Grants unapplied	0	0	0	0	0	0
Capital Reserves	(2,137)	(1,682)	(222)	180	582	983
Resource Centre Mgrs	(6,574)	(4,541)	(4,331)	(4,059)	(3,659)	(3,908)
Community Risk Reduction	(441)	(430)	(430)	(430)	(430)	(430)
UPG	(372)	(372)	(122)	(122)	(122)	(122)
Total earmarked reserves	(20,080)	(15,618)	(8,936)	(4,061)	(2,628)	(2,445)
General Reserve	(7,986)	(6,467)	(6,467)	(6,467)	(6,467)	(5,818)
Total usable reserves	(28,066)	(22,085)	(15,403)	(10,528)	(9,095)	(8,263)

13. Based on the anticipated levels of capital investment the reserves set aside for such purposes will be exhausted in 2019/20 as shown in the table above (red figures). As reserves run out, the main source of funding will have to be borrowing.

14. The Resource Centre Managers reserve covers a number of areas under the directions of the Heads of Department. The key areas are funds to support fire prosecutions; staff related – e.g. ill health pensions, training etc.; insurance; replacement of some operational equipment; ICT replacement; and property related costs.

BORROWING

Current loans

15. At the 31 March 2017, the Fire Authority held £1.9m of outstanding debt. Apart from one small loan of £22k which will be repaid shortly, the remaining loans are all maturity loans repayable at the end of the loan period. This is summarised in the table below.

Type of loan	Start Date	Maturity Date	Original Principal	Interest Rate
PWLB loan - Maturity	16/11/1999	31/03/2025	£467,000.00	4.2500
PWLB loan - Maturity	13/04/2000	31/03/2024	£426,000.00	4.8750
PWLB loan - Maturity	21/06/2002	31/03/2027	£119,000.00	5.3750
PWLB loan - Maturity	22/12/2005	31/03/2020	£880,000.00	4.3500
			£1,892,000.00	

Interest rates

16. Since the financial crisis, the Bank of England has reduced and maintained interest rates at historically low rates. Following the Brexit vote, the rate was reduced further to 0.25%. At the Bank of England Monetary Policy Committee on 2 November 2017, the base rate was increased by 0.25% to 0.5% (the rate prior to the Brexit vote). The Governor of the Bank of England has stated that this is the first step to raising interest rates but that this would move forward at a slow and steady pace.

17. Given the information above, it is clear that interest rates are going to rise albeit at a measured pace and with the level of reserves forecast to be fully utilised by 2022, with no annual capital grant funding, borrowing will be required – it is just a question of when.

Options for borrowing

18. The Public Works Loan Board (PWLB) is a statutory body that issues loans to local authorities, and other specified bodies, from the National Loans Fund. This is not the only option available – the Authority could borrow from the money market, banks etc., if one of those options offered value for money. At present, the PWLB offers favourable interest rates and the following shows the options available. There are three types of PWLB loans available:

   - Annuity (or Equal Repayments): fixed half-yearly payments to include principal and interest.
   - Equal Instalments of Principal (EIP): equal half-yearly instalments of principal together with interest on the balance outstanding at the time.
   - Maturity: half-yearly payments of interest only, with a single repayment of principal at the end of the term.

19. Based on the interest rates applicable on 20 November, the following shows the cost of each type of loan for the sum of £9m (the budget for the training centre project and associated works). For the maturity loan, an amount is set aside each year over the length of the loan to ensure sufficient cash is available at the end of the term to repay the loan, in line with the prudential requirements. For the other two types of loans, the payment made each year includes some repayment towards the capital so has reducing interest over the life of the loan.

			Total Interest	Per annum		Total Paid
Annuity	50 years	2.90%	£8,104,108	£342,082		£17,104,108
	40 years	2.92%	£6,315,254	£382,881		£15,315,254
	30 years	2.78%	£4,327,652	£444,255		£13,327,652
EIP	50 years	2.93%	£6,658,425	£442,382	reducing by £6k pa.	£15,658,425
	40 years	2.89%	£5,267,025	£558,474	reducing by £7k pa.	£14,267,025
	30 years	2.72%	£3,733,200	£542,760	reducing by £8k pa.	£12,733,200
Maturity	50 years	2.65%	£11,925,000	£418,500		£20,925,000
	40 years	2.71%	£9,756,000	£468,900		£18,756,000
	30 years	2.89%	£7,803,000	£560,100		£16,803,000

Financial Implications

20. Under the CIPFA Prudential Code adopted under the Treasury Management Strategy, the Authority has a right to borrow providing it is deemed prudent. The Prudential Indicators demonstrate this position and are reported to Members annually at the February Fire Authority meeting as well as at the mid-year review. The £9m borrowing meets the requirements of this code.

Legal Implications

21. The Authority has a legal right to borrow.

Equality and Diversity Implications

22. This report does not have any equality and diversity implications.

Environmental Implications

23. This report does not have any environmental implications.

Conclusion

24. Reserves are now fully committed and with the regular capital expenditure costing £1.5m to £2m every year, there is no funding available and borrowing becomes inevitable. Interest rates are currently at historically low levels and therefore, borrowing now offers the most cost effective option.

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BACKGROUND PAPERS: NONE