# ESSEX FIRE AUTHORITY
# Essex County Fire & Rescue Service

| | | | |
|---|---|---|---|
| **MEETING** | Audit, Governance & Review Committee | **AGENDA ITEM** | **7** |
| **MEETING DATE** | 7 October 2015 | **REPORT NUMBER** | **EFA/089/15** |
| **SUBJECT** | Investment Policy & Use of Reserves | | |
| **REPORT BY** | The Finance Director & Treasurer, Mike Clayton | | |
| **PRESENTED BY** | The Finance Director & Treasurer, Mike Clayton | | |

## SUMMARY

This paper brings forward a draft report on the Authority's cash and reserves position and seeks Member's views on the policy to be followed in respect of investment, cash holdings and reserves.

## RECOMMENDATION

Members of the Audit Sub Committee are asked to consider the report and determine whether any changes to the Authority's policy on investment, cash holdings and reserves are required.

## BACKGROUND

When the Authority considered the overall level of reserves as part of the budget setting process for 2015/16 it agreed to establish a sub-group of Members to review the policy to be followed in respect of investment, cash holdings and reserves. A meeting of the sub-group was held on 15 July 2015 but only one Member was able to attend. It was agreed to bring a report forward through the Audit, Governance and Review Committee as all Members of the sub-group sit on the Committee.

The Fire Authority or its Committees have made few changes to the Authority's policies concerning investment and reserves. The longest established position was adopted some 8 years ago when it was agreed that reserves would not be held as cash, but instead be used to reduce the borrowing requirements of the Authority. One impact of this policy is that the Authority currently has £33.5m of loans for around £100m of assets.

## DEBT PORTFOLIO

The present debt portfolio of the Authority consists of borrowings from the Public Works Loan Board (PWLB). These are listed in the table below:

| Start Date | Maturity Date | Original Principal | Interest Rate | Annual Interest Cost |
|---|---|---|---|---|
| 07/03/2008 | 01/01/2016 | £4,000,000 | 4.49 | £179,600 |
| 12/08/2009 | 31/08/2016 | £1,500,000 | 3.66 | £54,900 |
| 25/03/2010 | 25/03/2019 | £1,000,000 | 3.96 | £39,600 |
| 27/03/2009 | 31/08/2019 | £2,500,000 | 3.57 | £89,250 |
| 25/03/2010 | 25/03/2023 | £1,000,000 | 4.41 | £44,100 |
| 21/12/2004 | 01/03/2025 | £1,000,000 | 4.55 | £45,500 |
| 21/12/2004 | 01/11/2025 | £1,000,000 | 4.55 | £45,500 |
| 11/06/2007 | 01/08/2028 | £5,000,000 | 5.05 | £252,500 |
| 02/08/2007 | 01/05/2029 | £5,000,000 | 4.95 | £247,500 |
| 02/08/2007 | 01/09/2030 | £5,000,000 | 4.95 | £247,500 |
| 25/03/2010 | 25/03/2033 | £2,000,000 | 4.65 | £93,000 |
| 11/12/2009 | 11/12/2034 | £4,500,000 | 4.39 | £197,550 |
| | | | | |
| **Total** | | **£33,500,000** | **4.59** | **£1,536,500** |

No new loans have been entered into since March 2010 as the Authority has had sufficient cash balances to fund the level of capital expenditure. Changes to the rules concerning PWLB loans were made a few years ago and as a result there is no financial benefit in early repayment of a loan. This is because the full amount of interest due until the end of the loan period has to be paid.

**CASH MOVEMENTS**

In cash terms the Authority's accounts are generally fairly simple, with little movement in current assets and liabilities in most years. As a result, the movement in the cash balance is largely determined by the size of any revenue underspend (increases cash); the charge for capital financing (essentially historic cost depreciation that increases cash), capital receipts (increases cash) and capital expenditure (reduces cash). One exception is the provision in our 2013/14 accounts for the repayment to the government of pension injury payments – this liability remains on the Authority's balance sheet as no decision has yet been made by the government concerning the amount and timing of this repayment.

**INVESTMENTS**

The Authority considers on an annual basis the criteria for counter parties for the investment of surplus cash. At present we spread our investments between our main bank and a low risk money market fund (CCLA). Members' agreed to the use of the CCLA Property Fund in February 2015, this is a vehicle suitable for longer term investment. The present position is that the Authority has investments of £9m with Lloyds and £14.5m in the CCLA Money Market Fund.

**LOOKING AHEAD**

There are two areas that need to be considered in looking at the longer term position of the Authority. If there is a desire to build up a larger investment portfolio to provide income over the longer term then this will need to be achieved through either the sale of assets or running a surplus on the income and expenditure account. In the longer term the interest costs would need to exceed the interest rates on PWLB (or alternative) loans. A 2% margin above the loans on (say) £20m of investment would generate net income of £400k per annum.

There are other factors that will need to be considered. These include the potential revenue costs of changes to service design agreed as part of the 2020 programme, the potential for assets sales as a result of the programme and major capital expenditure need over the next few years at Service Workshops and some larger fire stations.

**CASH FORECASTS**

The current cash position with £23.5m invested is a short term position. The Authority has a provision of £13.3 in respect of amounts due to the government for pension injury payments. No decision by the government on the repayment of this amount has been made.

For the rest of 2015/16 the forecast outturn includes £7.9m of non-cash items in the income and expenditure accounts and £10.6m of capital spending. This suggests that cash balances will reduce by £2.7m to fund the planned level of capital spending. In addition there will be a repayment of £4m of PWLB loans.

In total these outflows amount to £20m, reducing the forecast cash position to £3.5m by the year end. Cash forecasts have been prepared to show the potential impact of these changes.

**2020 PROGRAMME**

The proposals for the 2020 programme have not yet been drawn up or agreed. There is a potential need for up-front funding for change measures that will need to be financed by cash. If cash forecasts are exceeded the Authority has the potential to borrow money to fund the capital programme in the current year, or the next financial year. In addition further cash receipts are expected in the current financial year from the sale of the former headquarters at Hutton, but the timing of this receipt remains uncertain.

**RISK MANAGEMENT, LEGAL, FINANCIAL, ENVIRONMENTAL & EQUALITY IMPLICATIONS**

There are no legal, environmental or equality implications from this report.

The financial implications are set out in the report.

The risk management implications centre on the trade-off between risk and reward in making investments, and the time period over which investments produce returns. At present the Authority has adopted a low risk strategy to managing its cash, with a preference not to hold reserves as cash, but to reduce borrowing. This approach has saved the Authority money. For example if the Authority borrowed £10m to fund the current years capital expenditure and invested £10m in a money market fund then costs would be up to £400k higher.

The other risk for the Authority is not having cash available to fund expenditure. This risk is managed through the cash forecasting process – the Finance department have a detailed forecast for the remainder of the financial year, and through the flexibility in borrowing to fund capital spending.