Buckinghamshire & Milton Keynes Fire Authority

MEETING	Fire Authority
DATE OF MEETING	17 December 2014
OFFICER	David Skinner, Director of Finance & Assets
LEAD MEMBER	Councillor Andy Dransfield
SUBJECT OF THE REPORT	**Interpreting the Accounts – Key Financial Ratios**
EXECUTIVE SUMMARY	In 2009, the Audit Commission highlighted financial reporting as an important tool to promote the accountability of public bodies for their spending decisions. A number of financial ratios were identified that help put aspects of local government finances, such as income, assets, debt and reserves, into context. These ratios could then be used by senior managers, elected Members and taxpayers to scrutinise and challenge financial management decisions based on the data in their accounts. The key financial ratios identified were; (i) Current assets to current liabilities (ii) Usable reserves to gross revenue (iii) Long-term borrowing to tax revenue (iv) Long-term borrowing to long-term assets The report at Appendix A details how these ratios can be used to examine financial performance. The report calculates the 2012/13 and 2013/14 ratios for Buckinghamshire and Milton Keynes Fire Authority (BMKFA) and compares the results with our constituent councils and districts; Buckinghamshire County Council (BCC), Milton Keynes Council (MK), Aylesbury Vale District Council (AVDC), Chiltern District Council (CDC), South Bucks District Council (SBDC) and Wycombe District Council (WDC). The initial analysis shows that the Authority is currently in a strong financial position. The Authority has already taken action to strengthen its position further, by ensuring that no additional borrowing is required to fund the ongoing capital programme. The ratios will strengthen as long-term borrowing is repaid in line with the maturity profile (there is currently no incentive to repay borrowing early due to the substantial early repayment premiums that would be incurred). Further work will be carried out to compare the ratios

	for BMKFA against all other combined fire authorities and reported to the Fire Authority in February 2015 as part of the budget and medium term financial plan papers.
ACTION	Information.
RECOMMENDATIONS	It is recommended that the report be noted.
RISK MANAGEMENT	Management of our financial resources is a key risk to the Authority. The use of ratio analysis to monitor performance can be used to inform Members of the main financial risks facing the Authority.
FINANCIAL IMPLICATIONS	No direct impact.
LEGAL IMPLICATIONS	No direct impact.
HEALTH AND SAFETY	No direct impact.
EQUALITY AND DIVERSITY	No direct impact.
USE OF RESOURCES	Ratio analysis can be used to interpret our financial performance and support accountability of resources required to deliver the objectives of the Authority.
PROVENANCE SECTION & BACKGROUND PAPERS	Interpreting the accounts – A review of local government financial ratios 2007/08 to 2012/13 [Audit Commission, September 2014] http://www.audit-commission.gov.uk/wp-content/uploads/2014/09/FR-briefing-final-22-Sept-2014.pdf
APPENDICES	Appendix A – Key Financial Ratios
TIME REQUIRED	10 minutes.
REPORT ORIGINATOR AND CONTACT	Graham Young gyoung@bucksfire.gov.uk 01296 744429

Appendix A – Key Financial Ratios

This appendix examines each of the key financial ratios in turn.

(i) Current assets to current liabilities

This ratio measures the relationship between an organisation's current assets and its current liabilities. While it is commonly used to examine whether organisations are able to pay their debts in the short term, this is unlikely to be a significant risk for local government organisations given their ability to take short-term borrowing (though there may be additional costs to organisations that rely on short-term borrowing to pay debts). It does, however, act as an indicator of how short-term finances are managed and highlight possible future cash-flow problems. If a local government organisation did experience cash-flow difficulties which resulted in, for example, problems paying creditors this could present a significant reputational risk to the organisation. Conversely, authorities with a high ratio, over 4.0, should possibly consider if they are managing their current assets in the most effective way.

Current assets include cash and cash equivalents, payments in advance, debtors, short-term investments, inventories, assets held for sale and current intangible assets.

Current liabilities include bank overdrafts, receipts in advance, creditors, short-term borrowing, provisions, liabilities held by groups awaiting disposal and other short-term liabilities (e.g. current finance lease liabilities).

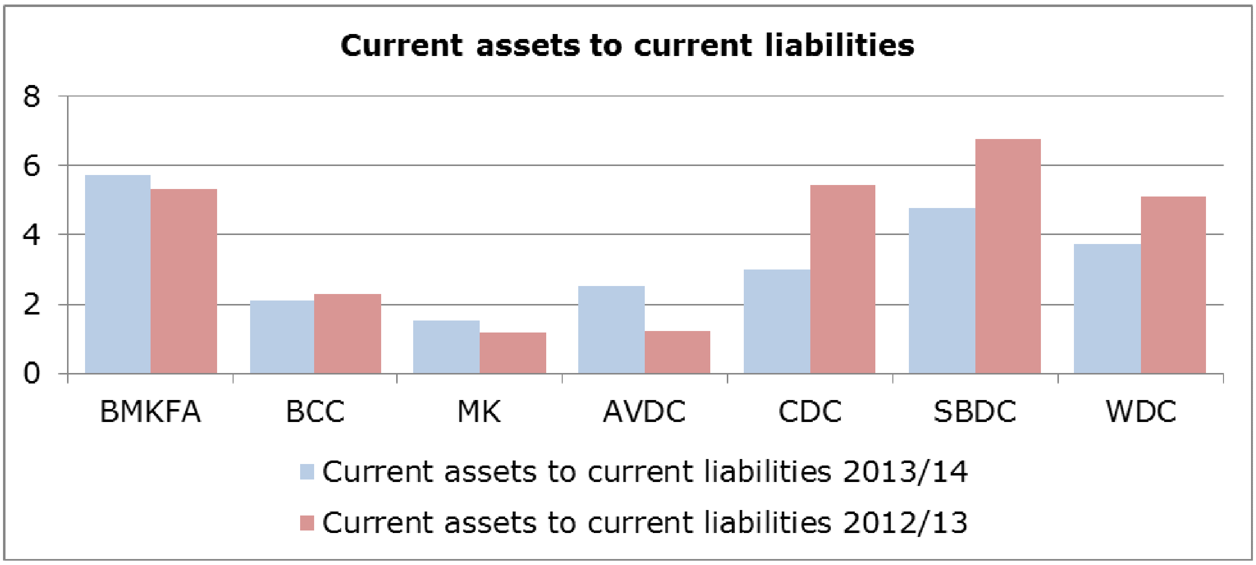

Chart 1

Chart 1 above shows that all the organisations have a ratio over 1.0 in both 2013/14 and 2012/13. This indicates that they have a higher level of current assets than current liabilities and are therefore managing their current assets effectively. BMKFA has the highest figure in 2013/14 with a ratio of 5.7. This high ratio is due to the number of short-term investments currently held in order to manage liquidity. This figure will reduce as cash is used to repay long-term borrowing in future years.

(ii) Usable reserves to gross revenue expenditure

This ratio measures the relationship between an organisation's usable reserves, which is the money it is retaining to fund future spending commitments and to meet unpredictable variations in spending, and its annual gross revenue expenditure. Organisations make local decisions on the amount of reserves they need in response to their local circumstances. Elected Members are responsible for ensuring that the levels of reserves are appropriate and the purposes for holding these reserves should be clearly communicated through the annual accounts. Authorities with very high levels of reserves relative to their spending should review the purposes for which these are held to ensure that they are still required.

Usable reserves include the General Fund, other earmarked reserves and usable capital receipts.

Gross revenue expenditure is the total cost of services shown in the comprehensive income and expenditure statement within the accounts.

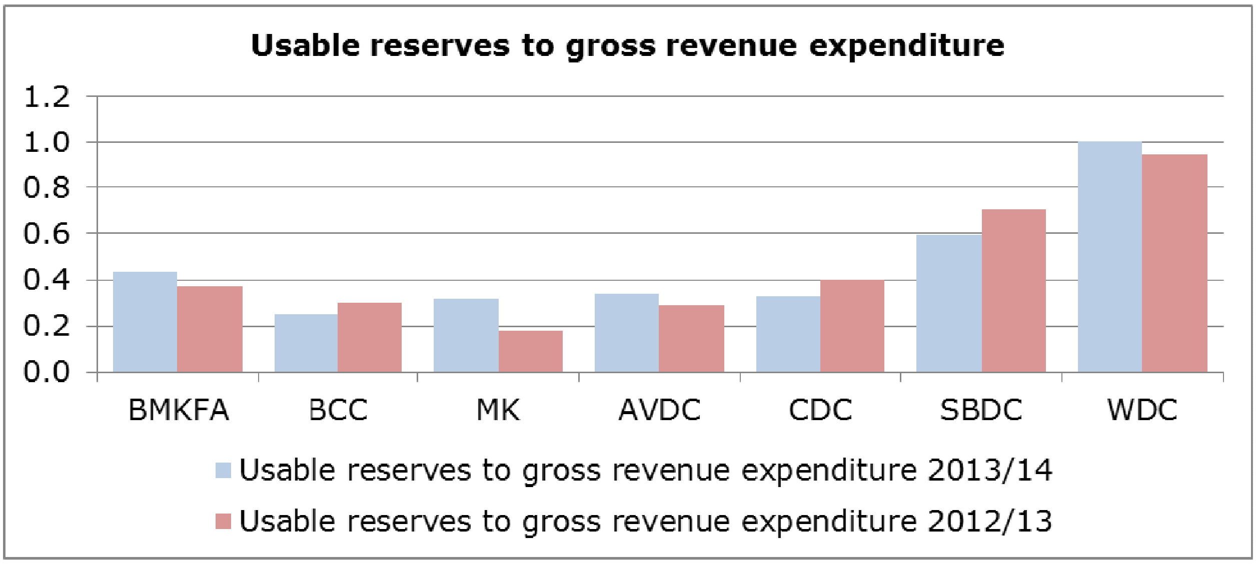

Chart 2

The usable reserves to gross expenditure ratios are shown in Chart 2. The reason for a high ratio here is generally as a consequence of a reduction in spending as organisations change the way they deliver services at lower cost, combined with increasing levels of reserves being held due to the uncertainty of future funding levels. The graph indicates that BMKFA are holding reserves of approximately 40% of gross revenue expenditure, which whilst fairly high, is in line with most of the other authorities. WDC have the highest ratio in both 2012/13 and 2013/14, with a ratio over 1.0 in the latter year, indicating that they currently hold in reserves more than 100% of their revenue spending.

(iii) Long-term borrowing to tax revenue

This ratio measures the relationship between an organisation's long-term borrowing and its tax revenue. When interpreting this ratio, consideration should be given to the reasons for long-term borrowing. Local government organisations enter into long-term borrowing to finance large-scale investment in the buildings and equipment they need to deliver services. Organisations need to ensure that their medium-term financial strategies take sufficient account of the level of debt repayments to minimise any impact these may have on future spending plans. Currently interest rates are at a historically low level, making borrowing more affordable, however, with interest rates set to rise in the years ahead, future borrowing will become more expensive.

Long-term borrowing includes long-term loans, long-term liabilities relating to Private Finance Initiatives and finance lease liabilities.

Tax revenue includes the revenue support grant, Council Tax income and business rates income (non-domestic rates).

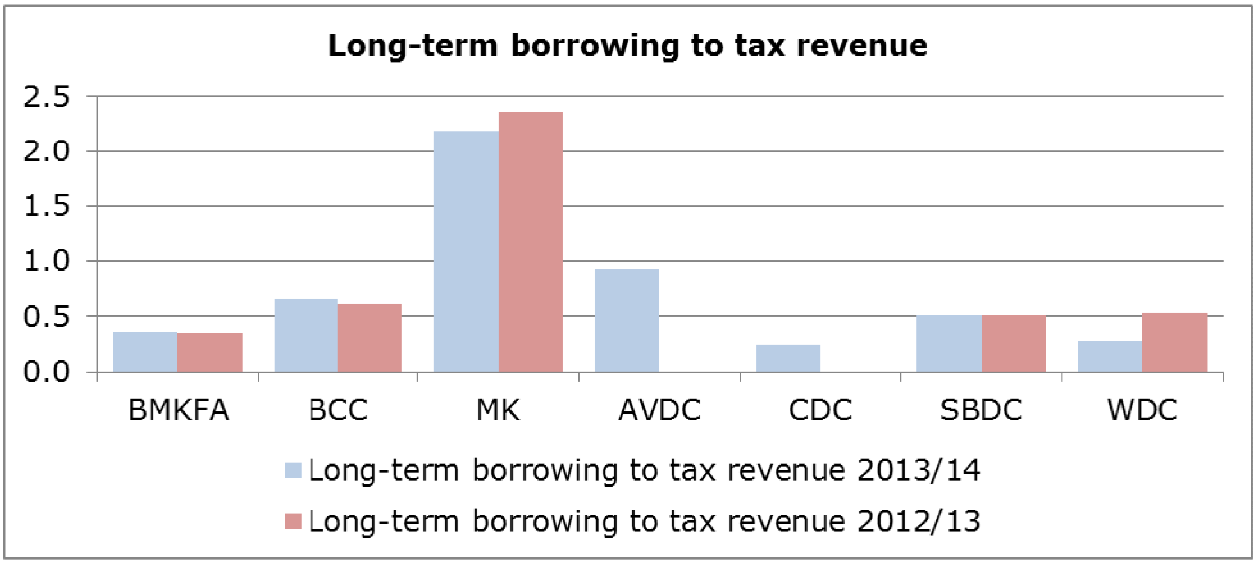

Chart 3

Chart 3 shows the long-term borrowing compared with tax revenues. The comparison below shows that BMKFA has a fairly low reliance on long-term borrowing with outstanding borrowing at approximately a third of tax revenue. This is primarily because in recent years the capital programme has been funded from capital grant and contributions from revenue. MK has the highest long-term borrowing when compared with tax revenues with over £400m in long-term debt in 2013/14 in respect of the funding of capital projects. Both AVDC and CDC had no long-term borrowings in 2012/13.

(iv) Long-term borrowing to long-term assets

This ratio measures the relationship between an organisation's long-term borrowing and long-term assets. This ratio provides insight into what borrowing has funded and the potential need for future borrowing to finance investment in delivering services. Once again, interpretation of this ratio requires consideration of the historical reasons for long-term borrowing. The amount that organisations need to borrow to finance their long-term capital investment plans will be influenced by their ability to raise funds from the sale of existing long-term assets.

Long-term borrowing includes long-term loans, long-term liabilities relating to Private Finance Initiatives and finance lease liabilities.

Long-term assets includes property, plant and equipment, heritage assets, investment property, intangible assets (e.g. computer software), assets under construction, long-term investments and long-term debtors.

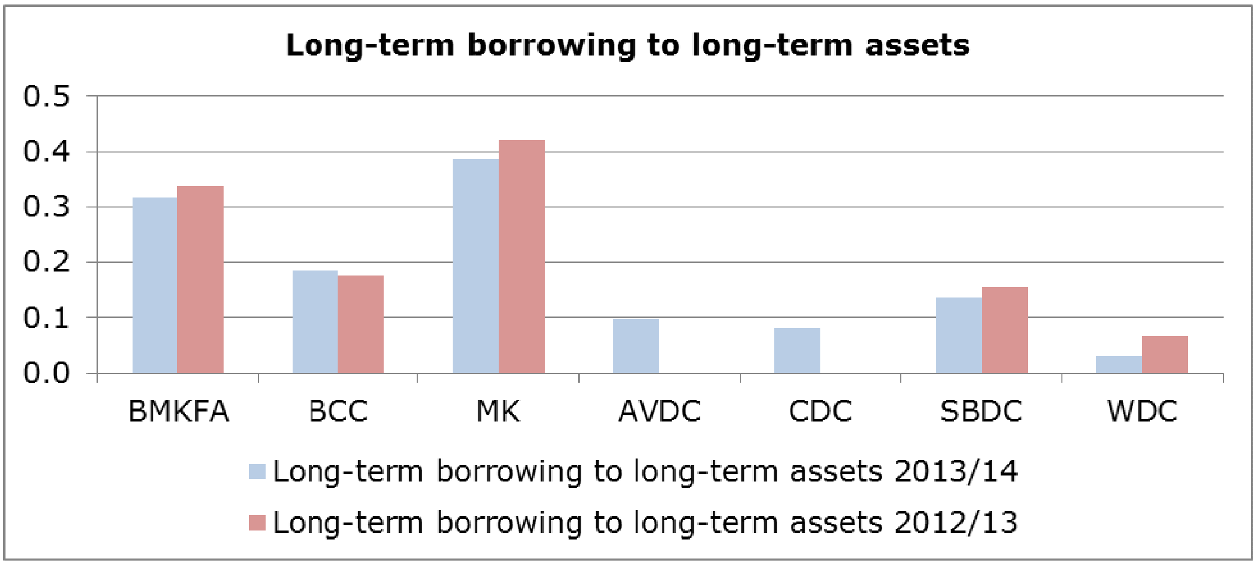

Chart 4

Chart 4 indicates how much outstanding borrowing each Authority has compared with their long-term assets. Currently BMKFA has outstanding borrowing equivalent to approximately a third of the value of its long-term assets. The Authority has no current plans to borrow further, instead funding future capital expenditure through revenue contributions. MK is shown as having the highest level of borrowing compared with long-term assets, again due to its high level of outstanding debt. Both AVDC and CDC had no long-term borrowings in 2012/13.