

RESERVES STRATEGY 2020-25

Background

1. The requirement for a local authority to maintain financial reserves is acknowledged in legislation: the Local Government Act 1992 requires billing and precepting authorities to have regard to the level of reserves needed for meeting estimated future expenditure when calculating the budget requirement.
2. In addition to holding financial reserves, there are a number of safeguards in place that mitigate against the risk of local authorities over committing themselves financially:
 - There is a legal requirement to set a balanced budget;
 - In accordance with the 1988 Local Government Finance Act the Chief Finance Officer (Section 151 Officer) must report if there is or is likely to be unlawful expenditure or an unbalanced budget. This would include situations where reserves have become seriously depleted and it is forecast that expenditure will exceed resources;
 - The external auditor's responsibility to review and report on financial standing.
3. While it is primarily the responsibility of Members and the Section 151 Officer to maintain a sound financial position, external auditors have a responsibility to review the arrangements in place to ensure that financial standing is soundly based. The work undertaken by external auditors will include a review of the level of reserves and the advice given to Members by the Chief Finance Officer.
4. The Fire and Rescue National Framework (May 2018) includes the requirement that fire authorities "should establish a policy on reserves and provisions in consultation with their Chief Finance Officer". It also requires that "fire authorities should publish their reserves strategy, including details of the current and future planned levels, the purpose for which each reserve is held and how each reserve supports the medium term financial plan".

Determining the level of reserves

5. In accordance with Financial Regulations, the Authority holds reserves which fall into two distinct categories:
 - General Reserves: these are necessary to fund any day to day cash flow requirements and also to provide a contingency in the event of any unexpected events or emergencies, and
 - Earmarked Reserves: these have been created for specific purposes and involve funds being set aside to meet known or predicted future liabilities.

Such reserves are intended to smooth the expenditure profile and avoid liabilities being met from Council Tax or the need to make offsetting savings in the year that expenditure is incurred.

6. There is not a standard recognised formula for determining the level of reserve that each local authority should maintain. It is up to each authority to consider the local circumstances and the potential issues/risks that may occur across the medium term. In determining an appropriate level of reserves for Cheshire Fire Authority the range of risks and issues that should be taken into account will include the following:
 - The possibility of additional savings being required in the future and the potential difficulty in delivering such savings. Future funding levels are unclear with only the 2020/21 funding known with any degree of certainty. If annual spending reductions were to continue or increase this may lead to the identification of savings proposals that may not prove to be deliverable;
 - To provide cover for extraordinary or unforeseen events occurring: given that the purpose of the fire and rescue service is to respond to emergency situations, there is always the potential for additional, unexpected and unbudgeted expenditure to occur;
 - The level of self insurance that we provide to minimise our insurance premiums: potential insurance liabilities can vary significantly across financial years. The levels of liabilities are difficult to accurately forecast and it would not be appropriate to budget for peak levels of expenditure.
 - The commitments falling on future years as a result of capital plans and proposals to improve/develop the asset held by the Authority. Having reserves would mitigate the impact on the revenue budget of borrowing and/or revenue contributions to capital and would support projects/programmes that will generate revenue efficiencies.
 - The risk of inflation – while the proposed 2020/21 budget and the Medium Term Financial Plan, includes an estimate for inflation, the level of pay awards or increase in costs may be significantly different.
 - Following the McCloud pension case, there will be significant costs relating to the remedy currently being reviewed by the Employment Tribunal. The actual funding of the remedy and compensation remains unknown but could impact on the Authority.

General Reserve

7. In recent years there has been considerable debate about the level of general reserves that are being held by local authorities. Whilst there is no specified minimum general reserve level, best practice has indicated that an appropriate and prudent level is one that is equivalent to 5% of the net revenue budget. This has been recommended in the past in Audit reports and has been included in

past comments by Government Ministers as being an accepted “reasonable level” of general reserve.

8. The Fire and Rescue National Framework requires that a Reserves Strategy should explain how the “level of general reserve has been set” and should include “justification for holding a general reserve larger than 5% of budget”. This therefore adds weight to the adoption of 5% of budget as an appropriate calculation of the required level of general reserve.
9. For Cheshire Fire Authority, the level of General Reserve at 31 March 2019 stood at £2.2m which is in line with 5% of the budget. As such, this Strategy states that if further revenue underspends occur – or if earmarked reserves are able to be released - that these are taken to Earmarked Capital Reserves to support the capital programme.
10. The table set out in the Annex summarises the position to 2025. This Strategy will be kept under review as capital spending is incurred and the level of reserves is adjusted to reflect the actual position at the end of each financial year.

Earmarked Reserves

11. The Fire Authority has a number of earmarked reserves. These have been set aside to support capital and revenue expenditure in future years. An annual review led by the Chief Fire Officer and Chief Executive and Senior Management Team is undertaken to ensure all earmarked reserves carried forward into the following financial year are still justified with clear plans for their usage. Details of the forecast levels of earmarked reserve are set out in Annex A. The forecast levels reflect the planned usage of reserves to meet anticipated expenditure. The main earmarked reserves are explained below.

IRMP Reserve

12. The purpose of this reserve is to meet the needs placed upon the Authority in meeting delivery programmes falling out of each IRMP. The reserve will be used over the next couple of years to finance the costs of some of the project teams that are implementing major capital projects and providing funding for temporary training facilities. Its continued use in supporting capital expenditure will mean the reserve will be fully depleted by 2025, unless there are additions from other reserves or revenue underspends.

Capital Reserve

13. The Government stopped providing capital grants to local authorities in 2014, although occasionally there are national initiatives announced that involve authorities bidding for grants in support of specific projects. The capital programme, including the training centre, new fire stations and the refurbishment plan, means the Authority now has a sizeable capital programme.

14. To keep borrowing to a minimum and avoid incurring the associated revenue expenditure, the strategy is to use contributions from reserves to fund the capital programme where possible.
15. As part of this strategy other earmarked reserves have been reviewed and where appropriate, taken to the capital reserve to support capital expenditure and to ensure that the capital reserve is not depleted entirely. However, it is recognised that the capital programme will cost more than the current reserves and it has already been agreed that borrowing will be required. Post 2025, when reserves have been generally fully used, further capital spend will be required to maintain or replace assets. Therefore a policy has been included within the Medium Term Financial Plan to provide an annual contribution to the capital reserve to fund the general annual asset replacement programme.

Resource Centre Reserve

16. This earmarked reserve is set aside to meet future identified commitments within the respective Resource Managers' areas. The amounts are attributable to the following issues/risks:

Employee related: there are a number of potential staff related issues that could result in additional costs. A significant cost is likely to arise as a result of the triennial review of the local government pension scheme: a sum has been set aside to meet potential costs of £0.32m in 2020/21. There is the potential for employee pay awards to be greater than that included in the revenue budget and for the actual number of firefighters to vary from the budgeted number, depending on the timing of employee movements. There are amounts held in the reserve to support potential expenditure should these risks materialise;

Legal and insurance: a balance of £0.7m is being maintained to meet any future prosecution and enforcement costs associated with the work of the protection team and to fund any successful claims which are self-insured;

ICT and systems development: approximately £0.6m is set aside to support ICT development work including any major system upgrades/replacements that may be required;

Training: approximately £0.3m is being earmarked for talent management and corporate training expenditure;

Equipment and uniforms: the balance on this reserve is reducing each year as it is used to meet the costs of new uniforms and new equipment, particularly protective equipment. By 2025 the balance on this reserve is forecast to be £0.5m;

Collaborations and partnerships: approximately £0.2m has been set aside to support the statutory duty to collaborate. The Authority has a number of collaboration initiatives including the North West Fire Control and Blue Light Collaboration with Cheshire Police;

Property related: a balance of £0.6m is being maintained to support property maintenance expenditure and to meet the costs of property related projects including environmental projects;

Prevention: there is a balance of £0.2m to support any future safety central marketing costs and a further £0.4m to incentivise the installation of sprinklers by social landlords.

Community Risk Reduction

16. Amounts have been set aside to support the cost of the Authority's Safe and Well Programme and other community safety activities. There is approximately £0.3m in this reserve and until further commitments are identified, this will be the balance to March 2025.

Unitary Performance Group (UPG)

17. Amounts have been set aside for facilitating partner engagement in community safety activities. This includes funding for the sprinkler campaign. It is forecast that by the end of 2019/20 there will be approximately £0.1m in this reserve and, until further commitments are identified, this will be the balance to March 2025.

Overall Position

18. One of the key elements of the Reserves Strategy will be to use the earmarked Capital and IRMP Reserves to support capital expenditure. The Capital Strategy for 2020 to 2025 indicates that expenditure of over £28m is planned to take place between 2020 and 2025 with approximately £18m of this being financed from reserves. The resulting balances on reserves are set out in Annex A below.

FORECAST LEVEL OF RESERVES TO MARCH 2025

	Forecast at	Forecast at	Forecast at	Forecast at	Forecast at	Forecast at
	31/03/2020	31/03/2021	31/03/2022	31/03/2023	31/03/2024	31/03/2025
	£000	£000	£000	£000	£000	£000
General Reserve	2,210	2,210	2,210	2,210	2,210	2,210
<u>Earmarked Reserves</u>						
IRMP	8,258	5,730	2,592	1,888	440	87
Capital	4,050	100	0	0	0	0
Resource Centre	4,991	4,265	4,197	4,133	3,647	3,646
Community Risk	329	329	329	329	329	329
UPG	101	101	101	101	101	101
TOTAL RESERVES	19,939	12,735	9,429	8,661	6,727	6,373