



## RESERVES AND BALANCES STRATEGY

2019/20 – 2022/23

## **Reserves and Balances Policy**

The National Framework published in December includes a section on reserves. The main components of which are:-

- General reserves should be held by the fire and rescue authority and managed to balance funding and spending priorities and to manage risks. This should be established as part of the medium-term financial planning process.
- Each fire and rescue authority should publish their reserves strategy on their website. The reserves strategy should include details of current and future planned reserve levels, setting out a total amount of reserves and the amount of each specific reserve that is held for each year. The reserves strategy should provide information for at least two years ahead.
- Sufficient information should be provided to enable understanding of the purpose for which each reserve is held and how holding each reserve supports the fire and rescue authority's medium term financial plan.
- Information should be set out in a way that is clear and understandable for members of the public, and should include:
  - how the level of the general reserve has been set;
  - justification for holding a general reserve larger than five percent of budget;
  - whether the funds in each earmarked reserve are legally or contractually committed, and if so what amount is so committed; and
  - a summary of what activities or items will be funded by each earmarked reserve, and how these support the fire and rescue authority's strategy to deliver good quality services to the public.

The reserves policy complies with these requirements.

### **General Reserves**

These are non-specific reserves which are kept to meet short/medium term unforeseeable expenditure and to enable significant changes in resources or expenditure to be properly managed in the medium term.

The Authority needs to hold an adequate level of general reserves in order to provide:-

- A working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing;
- A contingency to cushion the impact of unexpected events;
- A means of smoothing out large fluctuations in spending requirements and/or funding available.

The following table sets out the purpose of this reserve, how it is utilised, controlled and reviewed.

Name	General Fund
Purpose	This covers uncertainties in future years budgets, such as: <ul style="list-style-type: none"> <li>• future grant settlements being lower than forecast;</li> <li>• higher levels of inflation than budgeted;</li> <li>• increasing cost of and changes to pensions;</li> <li>• service demands increasing, putting additional pressure on demand led budgets;</li> <li>• changes in legislation impacting on future service provision;</li> <li>• potential cost of industrial action.</li> </ul>
Utilisation	This is utilised to offset any in-year overspend that would occur when comparing budget requirement to the level of funding generated.
Controls	The utilisation of this is agreed as part of the annual budget setting process. Any further utilisation requires the approval of the Resources Committee.
Review	The adequacy of this is reviewed annually, as part of the budget setting process.

### Review of Level of Reserves

In determining the appropriate level of general reserves required by the Authority, the Treasurer is required to form a professional judgement on this, taking account of the strategic, operational and financial risk facing the Authority. This is completed based on guidance issued by CIPFA, and includes an assessment of the financial assumptions underpinning the budget, the adequacy of insurance arrangements and consideration of the Authority's financial management arrangements. In addition the assessment should focus on both medium and long-term requirements, taking account of the Medium Term Financial Strategy.

For Lancashire Combined Fire Authority this covers issues such as: uncertainty surrounding future funding settlements and the potential impact of this on the revenue and capital budget; uncertainty surrounding future pay awards and inflation rates; the impact of changes to pension schemes; demand led pressures; risk of default associated with our investments as set out in the Treasury Management Strategy, cost associated with maintaining operational cover in the event of Industrial Action etc.

2019/20 is the final year of the current four year settlement. This means that funding beyond 2019/20 is subject to the outcome of next year's Spending Review, as well as the outcome of the fair funding review of relative needs and resources and the Government intention to move to greater retention of Business Rates, as opposed to maintaining Revenue Support Grant. Furthermore the impact of Brexit on the national economy is still unknown. Therefore there is greater degree of uncertainty over long term funding than in recent years.

As such the Treasurer considers it prudent to increase the minimum target reserves level to £3.2m, 5.7% of the 2019/20 net revenue budget, reflecting the increasing

level of uncertainty. This is broadly in line with the 5% threshold identified by the Home Office above which the Authority is required to justify why it holds the level of reserves.

Should reserves fall below this minimum level the following financial year's budget will contain options for increasing reserves back up to this level. (Note, this may take several years to achieve.)

Whilst this exercise sets a minimum level of reserves it does not consider what, if any, maximum level of reserves is appropriate. In order to do this the level of reserves held should be compared with the opportunity cost of holding these, which in simple terms means that if you hold reserves that are too high you are foregoing the opportunity to lower council tax or invest in further service improvements.

However, given the limited scope to increase council tax without holding a local referendum the ability to restore depleted reserves in future years is severely limited. Hence any maximum reserve limit must take account of future anticipated financial pressures and must look at the long term impact of these on the budget and hence the reserve requirement. Based on professional judgement, the Treasurer feels that this should be maintained at £10.0m.

Should this be exceeded the following financial year's budget will contain options for applying the excess balance in the medium term, i.e. over 3-5 years.

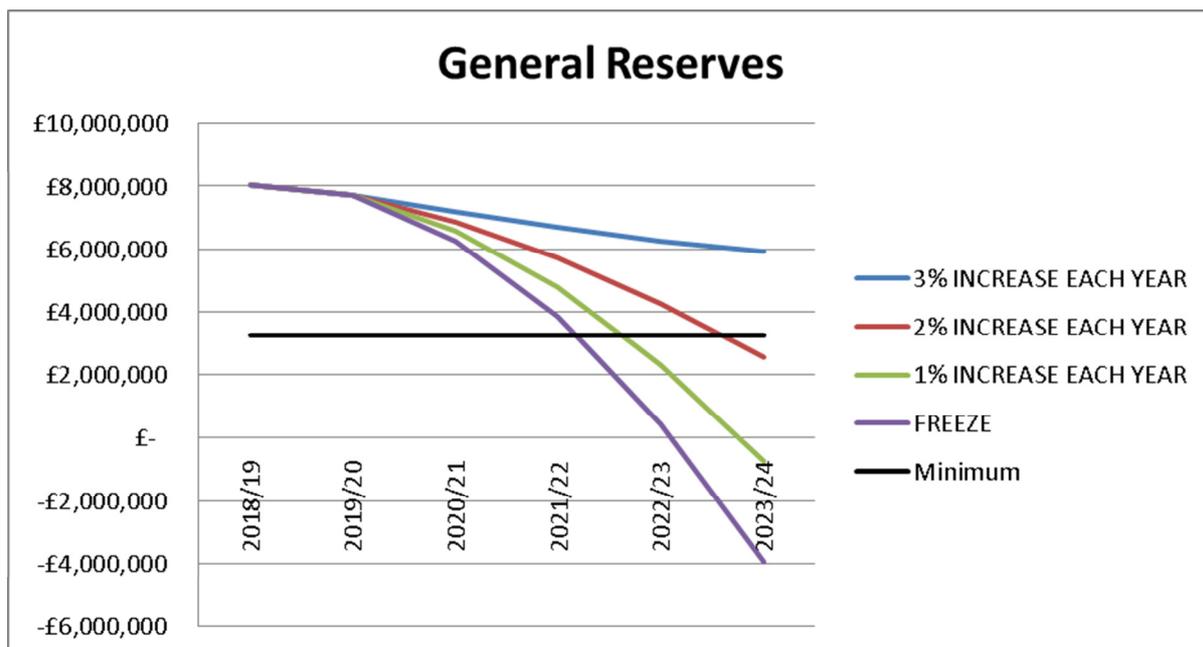
#### Level of General Reserves

The overall level of the general fund balance, i.e. uncommitted reserves, anticipated at the 31 March 2019 is £8.0m, providing scope to utilise approx. £4.8m of reserves.

The proposed drawdown of £0.3m in 19/20 would reduce the general balance to £7.7m and the Treasurer considers these are at an appropriate level to meet future expenditure requirements in 2019/20.

It should be noted that reserves are being used to fund recurring expenditure and hence this can only be a short term solution, with recurring savings being required in the longer term to offset the shortfall.

Future requirements are less clear as multi-year settlements will have ended and the budget forecasts become less accurate as there are a whole host of assumptions underpinning these projections, particularly around funding, vacancy profiles, pension costs, future inflation and pay awards and council tax increases. The following graph showing the point at which general reserves dip below minimum requirements, and the point at which they are exhausted, based on various council tax options.



As can be seen general reserves are sufficient to balance the budget next year. However they are only a short term solution, and based on the current assumptions included in the budget, even allowing for a 2% council tax increase each year, they will fall below our minimum level during 2023/24. Hence over the medium term the general reserve will potentially fall below the 5% threshold identified by the Home Office. Furthermore the utilisation of reserves will still leave a recurring funding gap that will need to be offset by savings at a future point in time, and as highlighted earlier the scope to do so is limited.

### Earmarked Reserves

These are reserves created for specific purposes to meet known or anticipated future liabilities and as such are not available to meet other budget pressures. They can only be used for that specific purpose, for which they were established, and as such it is not appropriate to set any specific limits on their level, but as part of the annual accounts process their adequacy will be reviewed and reported on.

The following table sets out the purpose of this reserve, how it is utilised, controlled and reviewed.

Name	Earmarked
Purpose	This covers monies set aside for specific purposes.
Utilisation	Once set up these reserves can only be used for the specific purpose for which they were established.
Controls	The utilisation of these are discussed at quarterly DFM meetings between the budget holder, relevant Executive Board member, and the Director of Corporate Services.
Review	The level of earmarked reserves is reviewed each year as part of the revenue outturn/annual accounts process to ensure these are reasonable and remain relevant.

The Director of Corporate Services has delegated authority to create new earmarked reserves valued at up to £100,000; any request which exceeds this must be reported to the Resources Committee for approval.

Specific earmarked reserves will be closed when there is no longer a requirement to hold them, at which point they will either hold a nil balance or when any outstanding balance will be transferred into the general reserve.

#### Level of Earmarked Reserves

The following table provides a breakdown of the £7.6m of earmarked reserves forecast to be held at 31st March 2019, and a forecast of the anticipated position as at 31 March 2024:-

	Forecast at 31 March 2019	Forecast at 31 March 2024	
	£m	£m	
DFM Reserve	0.3	0.2	<p>Devolved Financial Management Reserve enables budget holders to carry forward any surplus or deficit from one financial year to the next, within prescribed limits.</p> <p>The Service has strong financial management ethos and hence has a track record of managing within individual budget allocations, hence has not previously utilise these reserves to a large degree. However as the Service comes under increasing pressure and departmental budgets are squeezed this provides greater flexibility to individual budget holder and optimises the use of resources.</p> <p>Examples of areas where these balances have been used previously would be one off replacements of equipment, or enhancement to station facilities etc.</p> <p>The levels of individual DFM reserves are reviewed each year as part of the revenue outturn/annual accounts process, to ensure that they are reasonable and that budget holders are not building up excessive reserves.</p> <p>At present there are no contractual or legal obligations against this reserve, as any such commitments would be included in the base revenue budget.</p>
PFI Reserves	4.3	3.9	Private Finance Initiative Reserve, which is used to smooth out the annual net cost to the Authority of the existing PFI scheme, and will be required to meet future contract payments.

			<p>The utilisation of this is set out in the budget agreed at the start of the year, any variance in requirements from this are agreed by the Treasurer as part of the revenue outturn/annual accounts process.</p> <p>Assuming CPI continues at 3% the whole of this reserve is contractually committed over the next 20 years.</p>
Insurance Aggregate Stop Loss (ASL)	1.0	1.0	<p>The Authority has aggregate stop losses (ASLs) on both its combined liability insurance policy (£0.4m) and its motor policy (£0.3m). This means that in any one year the Authority's maximum liability for insurance claims is capped at the ASL. As such the Authority can either meet these costs direct from its revenue budget or can set up an earmarked reserve to meet these. Within Lancashire we have chosen to meet the potential costs through a combination of the two. Hence the amount included in the revenue budget reflects charges in a typical year, with the reserve being set up to cover any excess over and above this. As such the reserve, combined with amounts within the revenue budget, provides sufficient cover to meet 2 years' worth of the maximum possible claims, i.e. the ASL. (It is worth noting that the revenue budget allocation has also been reduced in recent years reflecting the claims history. Without holding this reserve to cushion any major claims that may arise this would not have been possible. )</p> <p>None of this reserve is legally committed at the present time, although as soon as a claim arose this position would change.</p>
PWLB Loan repayment penalty	0.9	0.9	<p>This reserve was created to meet the potential penalty costs associated with repayment of the remaining PWLB loans.</p> <p>The Authority still has £2.0m of long term loans, maturing between 2035 and 2037, as set out in the Treasury Management Strategy reported elsewhere on this agenda, and currently incurs £0.1m of interest charges on these loans. We continue to review opportunities to repay these, hence saving any interest payments, however based on the current penalty associated with this, £0.9m, it is not considered prudent to do so at the present time.</p> <p>There is no legal or contractual commitment</p>

			<p>against this reserve.</p> <p>It is worth noting that this is a notional amount as any penalties incurred will depend on both forecast interest rates and the remaining time to maturity, hence the actual penalty will be considered as part of the decision to repay the loans in due course, with any such decision being considered as part of future Treasury Management Strategy.</p> <p>Should Members decide to relocate SHQ, and hence agree to maintain the existing loans until maturity, the reserve could be used to offset some of the capital costs associated with the relocation.</p>
Prince's Trust	0.2	0.2	<p>This reserve has been established to balance short term funding timing differences and also to mitigate the risk of loss of funding and enable short term continuation of team activities, whilst alternative funding is found.</p> <p>The reserve is equivalent to 25% of the Teams current external funding target.</p> <p>Without this reserve any significant loss of funding would have an immediate impact on our ability to deliver the PT programme, and hence improve the lives of younger people.</p> <p>There are no legal or contractual commitments against this.</p>
ESMCP Ring-fenced Funding	0.1	-	<p>As part of the Emergency Services Mobile Communication Programme (ESMCP), transitional funding was made available to fund costs associated with the transition to the new national arrangements, with any funds not spent being carried forwards for use in future years.</p> <p>Whilst there are no contractual or legal commitments against this at the present time, the on-going programme will require this funding to be utilised in the new financial year</p>
Apprentices	0.1	-	<p>This reserve was created from previous the in-year underspends relating to the appointment of apprentices, which was delayed awaiting national developments.</p> <p>As such the reserve was set up to offset some of the pay costs that will be incurred in future years, with the balance being met direct from the revenue budget.</p> <p>There are no contractual commitments against this.</p> <p>This clearly contributes to addressing apprenticeship targets, set by the</p>

			Government, as well as addressing capacity issues within departments.
Fleet & Equipment	0.2	-	This reserve was created to meet the cost of replacement projects which were not completed by year end, hence whilst we anticipate carrying some over into 19/20 this will be fully utilised in that year At the present time £50k of the reserve is contractually committed.
Innovation Fund	0.5	-	The Authority created an Innovations Fund to meet costs arising from new initiatives/developments which improve service delivery or fire fighter safety but which are not included in the capital programme. Any requests to utilise the fund require the approval of the Executive Board. None of this reserve is contractually or legally committed at the present time.
	<b>7.6</b>	<b>6.2</b>	

It is worth noting that of the anticipated balance of £6.2m at 31 March 2024 over half of this relates to the PFI reserve.

Based on this the Treasurer believes these are adequate to meet future requirements in the medium term.

### **Capital Reserves and Receipts**

Capital Reserves have been created from under spends on the revenue budget in order to provide additional funding to support the capital programme in future years; as such they cannot be used to offset any deficit on the revenue budget, without having a significant impact on the capital programme that the Authority can support.

Capital Receipts are generated from the sale of surplus assets, which have not yet been utilised to fund the capital programme. Under revised regulations receipts generated between April 2016 and March 2019 can be used to meet qualifying revenue costs, i.e. set up and implementation costs of projects/schemes which are forecast to generate on-going savings. The on-going costs of such projects/schemes do not qualify. Whilst the Authority currently holds £1.6m of capital receipts only £140k of this arose in the relevant time period. Given the small amount eligible we do not currently have any plans to use this in line with new regulations and hence for the purpose of planning all capital receipts will be used to meet future capital costs, not qualifying revenue expenditure.

The following table sets out the purpose of this reserve, how it is utilised, controlled and reviewed.

<b>Name</b>	<b>Capital reserves and receipts</b>
Purpose	This covers monies set aside to fund the future capital programme.
Utilisation	Once set up these reserves can only be used to fund capital expenditure
Controls	The proposed utilisation of these is reported to the Authority as part of the capital programme setting and monitoring arrangements.
Review	These are reviewed on an annual basis as part of the year end outturn, reported to Resources Committee and as part of the capital budget setting report to the Authority.

At 31 March 2019 the Authority anticipates holding £18.2m of capital reserves and receipts. Based on the capital programme presented elsewhere on this agenda we anticipate utilising £16.2m by 31 March 2024. This leaves a balance of £2.0m to fund future capital programmes. Of the total reserve £1.8m is contractually committed.

Based on this the Treasurer believes these are adequate to meet future requirements in the medium term.

It should be noted that no allowance has been built in the capital programme for the potential relocation of SHQ. If this was included in the 5 year capital programme then all capital reserves and receipts would be utilised to fund this, as well as requiring additional borrowing.

## **Provisions**

The Authority has two provisions to meet future estimated liabilities:-

### Insurance Provision

This covers potential liabilities associated with outstanding insurance claims. Any claims for which we have been notified and where we are at fault will result in a legal commitment, however as the extent of these cannot be accurately assessed at the present time this provision is created to meet any element of cost for which we are liable, i.e. which are not reimbursable from insurers as they fall below individual excess clauses and the annual self-insured limits. This provision fully covers all estimated costs associated with outstanding claims.

The following table sets out the purpose of this provision, how it is utilised, controlled and reviewed.

<b>Name</b>	<b>Insurance Provision</b>
Purpose	This covers monies set aside to meet future insurance claims.
Utilisation	Once set up the provision can only be utilised to meet insurance claims.
Controls	The utilisation of these are reported on an annual basis as part of the year end outturn report presented to Resources Committee.

Review	The level of the provision is reviewed annually based on existing and anticipated outstanding insurance claims to ensure these are reasonable and remain relevant.
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This provision stood at £0.5m at 31 March 2018. Given the uncertainty in terms of future insurance claims we have assumed that the provision will be maintained at this level throughout the 5 year period. There are no existing legal obligations associated with this provision, as the legal obligation only arises when settlement of outstanding claims is agreed.

#### Business Rates Collection Fund Appeals Provision

This covers the Authority's share of outstanding appeals against business rates collection funds, which is calculated each year end by each billing authority within Lancashire based on their assumptions of outstanding appeal success rates, as part of their year-end accounting for the business rates collection fund.

The following table sets out the purpose of this provision, how it is utilised, controlled and reviewed.

Name	Business Rates Collection Fund Appeals Provision
Purpose	This covers monies set aside to meet the Authority's share of the cost of successful business rates appeals.
Utilisation	Once set up the provision can only be utilised to meet costs associated with settlement of such appeals.
Controls	The utilisation of these are reported on an annual basis as part of the year end outturn report presented to Resources Committee.
Review	The level of the provision is reviewed annually based on each billing authority's assumptions regarding success rates to ensure these are reasonable and remain relevant.

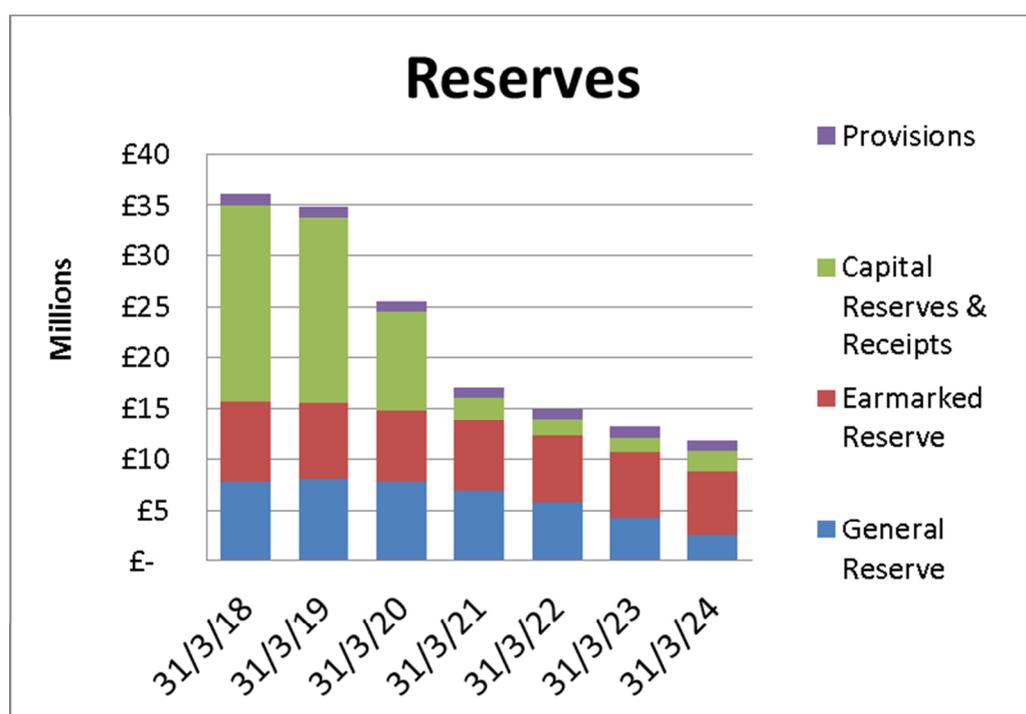
At 31 March 2018 this provision stood at £0.6m to cover anticipated costs of outstanding business rates appeals. Whilst a significant element of this will be utilised in the current financial year, reflecting the settlement of outstanding appeals, it is impossible to accurately predict the extent of this usage or the need for any additional provision to meet appeals that arise in year, until such time as a full review is undertaken as part of the financial year end process. Therefore for the purpose of this report we have assumed that the level of business rates appeals provision remains unchanged. Until the outcome of any appeal is known there is no legal obligation arising from the appeal.

The Treasurer feels that the level of provisions are sufficient to meet future requirements in the medium term.

#### **Summary Reserve Position**

The following table sets out the summary anticipated position in terms of reserves and balances showing the overall level reducing to approx. £12m by 31 March 2024:-

	General Reserve	Earmarked Reserve	Capital Reserves & Receipts	Provisions	Total Reserves & Balances
	£m	£m	£m	£m	£m
Balance 31/3/18	7.8	7.9	19.3	1.1	36.1
Change in year	0.2	(0.3)	(1.2)	(0.0)	(1.3)
Balance 31/3/19	8.0	7.6	18.2	1.1	34.8
Change in year	(0.3)	(0.4)	(8.4)	0.0	(9.2)
Balance 31/3/20	7.7	7.1	9.7	1.1	25.6
Change in year	(0.9)	(0.2)	(7.5)	0.0	(8.6)
Balance 31/3/21	6.9	6.9	2.3	1.1	17.1
Change in year	(1.2)	(0.3)	(0.7)	0.0	(2.1)
Balance 31/3/22	5.7	6.6	1.6	1.1	15.0
Change in year	(1.5)	(0.2)	(0.1)	0.0	(1.8)
Balance 31/3/23	4.3	6.4	1.4	1.1	13.2
Change in year	(1.7)	(0.2)	0.6	0.0	(1.3)
Balance 31/3/24	2.5	6.2	2.0	1.1	11.8



As this shows up to 31/3/2020, the end of the current multi-year settlement period, we remain in a healthy position. The reduction in the level of reserves becomes more of a concern thereafter with general reserves potentially falling below the minimum target level, but this position will be subject to significant change as funding, inflation, pay awards and other pressures all become clearer in future years. The annual refresh of this policy will identify the impact of any changes as they develop.

For comparative purposes the average level of reserves relative to total revenue expenditure across all Fire Authorities as at 31 March 2018 was 42%. Our anticipated position at the end of the current financial year shows reserves equal to 60% our revenue expenditure. However within this are £13m of capital slippage and a further £4m of PFI reserve, if we exclude these total reserves equate to £17m, 30% of our total revenue expenditure which is below the sector average.

It is also worth noting the comparator with other types of Authorities as set out in the Revenue Outturn Summary for 2017/18 comparing Net Revenue Expenditure with Non School Reserves:-

• London Boroughs	51%
• Metropolitan Districts	40%
• Unitary Authorities	39%
• Shire Counties	28%
• Shire Districts	144%
• Other (which includes Fire)	31%
• Overall	<u>40%</u>

Further details of the year on change in reserves is shown below:

	31/03/2018	31/03/2019	31/03/2020	31/03/2021	31/03/2022	31/03/2023
	£m	£m	£m	£m	£m	£m
<b>General</b>	<b>8.0</b>	<b>7.7</b>	<b>6.9</b>	<b>5.7</b>	<b>4.3</b>	<b>2.5</b>
<b>Earmarked</b>						
DFM	0.3	0.2	0.2	0.2	0.2	0.1
PFI	4.3	4.2	4.2	4.1	4.0	3.9
Insurance ASL	1.1	1.1	1.1	1.1	1.1	1.1
PWLB Loan Penalty	0.9	0.9	0.9	0.9	0.9	0.9
Equip	0.2	-	-	-	-	-
Princes Trust	0.2	0.2	0.2	0.2	0.2	0.2
ESMCP	0.1	- 0.0	- 0.0	- 0.0	- 0.0	- 0.0
Apprentices	0.2	0.1	0.1	-	-	-
Innovation Fund	0.5	0.4	0.3	0.2	0.1	-
	<b>7.6</b>	<b>7.1</b>	<b>6.9</b>	<b>6.6</b>	<b>6.4</b>	<b>6.2</b>
<b>Capital Reserves &amp; Receipts</b>	<b>18.2</b>	<b>9.7</b>	<b>2.3</b>	<b>1.6</b>	<b>1.4</b>	<b>2.0</b>
<b>Provisions</b>						
Insurance	0.5	0.5	0.5	0.5	0.5	0.5
Business Rate Collection Fund Appeals	0.6	0.6	0.6	0.6	0.6	0.6
	<b>1.2</b>	<b>1.2</b>	<b>1.2</b>	<b>1.2</b>	<b>1.2</b>	<b>1.2</b>
	<b>34.9</b>	<b>25.7</b>	<b>17.2</b>	<b>15.1</b>	<b>13.3</b>	<b>11.9</b>