



Nottinghamshire

POLICE & CRIME COMMISSIONER

Reserves Strategy 2015-16

Reserves Strategy 2015-16

Background

1. The requirement for financial reserves is acknowledged in statute. Sections 32 and 43 of the Local Government Act require precepting authorities (and billing authorities) in England and Wales to have regard to the level of reserves needed for meeting estimated future expenditure when calculating the budget requirement.
2. In England and Wales, earmarked reserves remain legally part of the General Reserve, although they are accounted for separately.
3. There are other safeguards in place that help to prevent Police & Crime Commissioners over-committing themselves financially. These include:
 - The balanced budget requirement (Local Government Act 1992 s32 and s43).
 - Chief Finance Officers duty to report on the robustness of estimates and adequacy of reserves (Local Government Act 2003 s25) when the Police & Crime Commissioner is considering the budget requirement.
 - Legislative requirement for each Police & Crime Commissioner to make arrangements for the proper administration of their financial affairs and that the Chief Finance Officer has responsibility for the administration of those affairs (section 151 of the Local Government Act 1972).
 - The requirements of the Prudential Code
 - Auditors will consider whether audited bodies have established adequate arrangements to ensure that their financial position is soundly based.
4. These requirements are reinforced by section 114 of the Local Government Finance Act 1988, which requires the Chief Finance Officer to report to the Police & Crime Commissioner if there 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 the Commissioner will not have the resources to meet its expenditure in a particular financial year. The issue of a section 114 notice cannot be taken lightly and has serious operational implications. Indeed, the Police & Crime Commissioner must consider the s114 notice within 21 days and during that period the Force is prohibited from entering into new agreements involving the incurring of expenditure

5. Whilst it is primarily the responsibility of the Police & Crime Commissioner and its Chief Finance Officer to maintain a sound financial position, external auditors will, as part of their wider responsibilities, consider whether audited bodies have established adequate arrangements to ensure that their financial position is soundly based. However, it is not the responsibility of auditors to prescribe the optimum or minimum level of reserves for individual Police and Crime Commissioners or authorities in general.
6. CIPFA's Prudential Code requires the Chief Finance Officers to have full regard to affordability when making recommendations about the Commissioners future capital programme. Such consideration includes the level of long-term revenue commitments. Indeed, in considering the affordability of its capital plans, the Commissioner is required to consider all of the resources available to it/estimated for the future, together with the totality of its capital plans and revenue forecasts for the forthcoming year and the following two years. There is a requirement for three-year revenue forecasts across the public sector and this is achieved through the Medium Term Financial Plan (MTFP). The Comprehensive Spending Review (CSR) has provided the Commissioner with details of proposed revenue grant for one year and capital grant settlement has yet to be announced. This provides limited ability to focus on the levels of reserves and application of balances and reserves.
7. CIPFA and the Local Authority Accounting Panel do not accept that there is a case for introducing a generally acceptable minimum level of reserves. Commissioners on the advice of their Chief Finance Officers should make their own judgements on such matters taking into account all relevant local circumstances. Such circumstances will vary between local policing areas. A well-managed organisation, for example, with a prudent approach to budgeting should be able to operate with a level of general reserves appropriate for the risks (both internal and external) to which it is exposed. In assessing the appropriate level of reserves, a well-managed organisation will ensure that the reserves are not only adequate, but also are necessary.
8. Section 26 of the Local Government Act 2003 gives Ministers in England and Wales a general power to set a minimum level of reserves for authorities. However, the government has undertaken to apply this only to individual authorities in the circumstances where the authority does not act prudently, disregards the advice of its Chief Finance Officer and is heading for serious financial difficulty. This would also apply to Police & Crime Commissioners. This accords with CIPFA's view that a generally applicable minimum level is appropriate, as a minimum level of reserve will be imposed where an authority is not following best financial practice.

Current Financial Climate

9. The pressures on public finances currently and for the medium term are intense. Therefore, the ability to retain reserves for unforeseen events and circumstances becomes not only difficult, but something that requires careful consideration.
10. Over the past few years the total amount held in reserves has increased due to year on year underspends. The amount now held in reserves is comparable with the national average. During 2014-15 an estimated £2m will be used from reserves in line with approvals made by the Commissioner during the year; with a further estimated £1m being required in to meet the shortfall in required efficiencies in year. It is currently anticipated that £3.0m will be required to set a balanced budget for 2015-16.
11. The Medium Term Financial Plan identifies risks in achieving the required savings to ensure balanced budgets over future years. Specifically there are early indications that the next CSR will require managing the finances with a further 20% reduction in grant funding this will probably see the need for reserves to be used and managed effectively.

Types of Reserve

12. When reviewing the medium term financial plans and preparing the annual budgets the Commissioner should consider the establishment and maintenance of reserves. These can be held for four main purposes:
 - A working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – this forms part of general reserves.
 - A contingency to cushion the impact of unexpected events or emergencies – this also forms part of general reserves.
 - A means of building up funds often referred to as earmarked reserves, to meet known or predicted requirements; earmarked reserves are accounted for separately, but remain legally part of the general reserve.
 - The economic climate and the safety of the Commissioner's financial assets. This would link closely with the Treasury Management and Prudential Code Strategy.
13. The Commissioner also holds other reserves that arise out of the interaction of legislation and proper accounting practice. These reserves are not resource-backed and cannot be used for any other purpose, are described below:

- The Pensions Reserve – this is a specific accounting mechanism used to reconcile the payments made for the year to various statutory pension schemes.
 - The Revaluation Reserve – this is a reserve that records unrealised gains in the value of fixed assets. The reserve increases when assets are revalued upwards, and decreases as assets are depreciated or revalued downwards or disposed of.
 - The Capital Adjustment Account – this is a specific accounting mechanism used to reconcile the different rates at which assets are depreciated under proper accounting practice and are financed through the capital controls system.
 - The Available-for-Sale Financial Instruments Reserve – this is a reserve that records unrealised revaluation gains arising from holding available-for-sale investments, plus any unrealised losses that have not arisen from impairment of the assets.
 - The Financial Instruments Adjustment Reserve – this is a specific accounting mechanism used to reconcile the different rates at which gains and losses (such as premiums on the early repayment of debt) are recognised under proper accounting practice and are required by statute to be met from the General Fund.
 - The Unequal Pay Back Pay Account – this is a specific accounting mechanism used to reconcile the different rates at which payments in relation to compensation for previous unequal pay are recognised under proper accounting practice and are required by statute to be met from the general fund.
 - Collection Fund Adjustment account – this is specific to the changes in accounting entries relating to the Collection Fund Accounts held by the Billing Authorities.
 - Accumulated Absences Account – this account came into being with the implementation of IFRS and represents the value of outstanding annual leave and time off in lieu as at 31st March.
14. Other such reserves may be created in future where developments in local authority accounting result in timing differences between the recognition of income and expenditure under proper accounting practice and under statute or regulation, such as the Capital Grants Unapplied.

15. In addition the Commissioner will hold a Capital Receipts Reserve. This reserve holds the proceeds from the sale of assets, and can only be used for capital purposes in accordance with the regulations.
16. For each earmarked reserve held by the Commissioner there should be a clear protocol setting out:
 - The reason for/purpose of the reserve
 - How and when the reserve can be used
 - Procedures for the reserves management and control
 - A process and timescale for review of the reserve to ensure continuing relevance and adequacy
17. When establishing reserves, The Commissioner needs to ensure compliance with the Code of Practice on Local Authority Accounting and in particular the need to distinguish between reserves and provisions.

Nottinghamshire Police & Crime Commissioner's Reserves

18. This document aims to provide an over-arching strategy that defines the boundaries within which the approved budget and Medium Term Financial Plan (MTFP) operate.

The General Reserve

19. It has previously been established that General Reserves will be maintained at a level above the minimum of 2.0% of the total net budget.
20. The purpose of this reserve is to provide for any unexpected expenditure that cannot be managed within existing budgets. Such expenditure would be one-off and resulting from an extraordinary event.
21. Similarly the General Reserve should be set at a prudent and not excessive level, as holding high level of reserves can impact on resources and performance. As such the maximum level of General Reserves is 5.0% of the total net budget.
22. Authorisation to finance such expenditure must be obtained in advance from the Commissioners Chief Finance Officer, in accordance with the scheme of delegation and the protocol between the Chief Constable and the Chief Finance Officer. Where time permits the request should be supported by a business case.

23. As the net budget position changes the level of General Reserve must be monitored to ensure the minimum level is maintained.
24. **Appendix A** details the elements that make up the current General Reserves balance and the levels of risk attached to each of these elements. These are indicative and may not be exhaustive as new risks emerge. This does not include the Jointly Controlled Operations general reserve of £0.074m.

Earmarked Reserves

25. Unlike General Reserves earmarked reserves have been identified for specific areas of expenditure where there are anticipated costs that can only be estimated. It is therefore prudent for the Commissioner to identify such areas of expenditure and set aside amounts that limit future risk exposure (e.g. balancing budget shortfalls in the MTFP).
26. Such expenditure usually arises out of changes in policy or where the organisation is working in collaboration with other forces to provide a specific service (for example Public Finance Initiative (pfi)).
27. Expenditure relating to earmarked reserves has to specifically relate to the purpose of the reserve.
28. **Appendix B** details for each of the earmarked reserves that existed at the start of the 2014-15 financial year and their estimated balance by 31st March 2015.

Details of those available for use in 2015-16 are given below:

Medium Term Financial Plan (MTFP) Reserve

29. The medium term financial plan of the Commissioner is under constant review and changes as new and reliable information becomes available.
30. The original purpose of this reserve is to alleviate financial pressure on the budgets in future years.
31. The support from this reserve is only one-off support and as such cannot be used to finance ongoing commitments.
32. The previously agreed strategy for utilising this reserve has been reviewed in light of the Comprehensive Spending Review and as such this reserve will

now be utilised to finance the cost of organisational changes and as an investment to facilitate new savings. In addition to this the reserve will also be utilised smooth budget pressures as they arise.

33. The Precept and Budget Reports that will be approved in February 2015 show a predicted under funding against budget of £0.9m in 2014-15 and a potential over funding against estimate of £0.7m in 2015-16. It is agreed that the MTFP reserve would meet the additional expenditure in 2014-15 and that the additional funding in 2015-16 will be transferred to reserves. All reserves will be utilised with the agreement of the Police & Crime Commissioner in the ways identified in this strategy and supported by a detailed business case.
34. The Medium Term Financial Plan has a risk assessment in relation to achieving the efficiencies identified. As such this reserve may be used for balancing the accounts should the efficiencies not be realised. Before considering the use of reserves recruitment will need to be slowed down or stopped.
35. **Appendix C** shows how the remainder of this reserve has been initially allocated over the next four years. It should be noted that there is a shortfall between budget and funds available in 2016-17, 2017-18 and 2018-19, which may require the use of reserves to finance all or part of the shortfall, depending on the level of further savings that can be achieved. No estimate has been included at this stage.

PCC Transition

36. Initially this was set up as a prudent measure to cover the costs known and unknown associated with the transition from Police Authority governance to governance by the Police & Crime Commissioner. The costs were kept to a minimum and totalled £54k.
37. Subsequently, this reserve is being used for Stage 2 transition costs. These are currently estimated to be £50k approximately.

Grants & Commissioning Reserve

38. It is intended that underspends on the OPCC budget and the Grants and Commissioning budget are swept into here to provide for future needs in this growing area of work.

Public Finance Initiative (PFI) Reserve

39. This is a reserve for the possibility of an extraordinary event relating to this significant contract. This is a prudent reserve to maintain.

Jointly Controlled Operations (Regional Collaboration) Reserve

40. There are a growing number of areas where collaborative working is undertaken with other Regional Policing areas. EMSOU is providing collaboration for specialised policing services, such as Major Crime and Forensics. Collaboration has also extended beyond Police Operation Services to include areas such as Legal Services, Procurement and Learning and Development.
41. The Police & Crime Commissioners meet to make decisions and agree further areas of collaboration. They would also approve the use of this reserve for regional activity.
42. The reserve exists to finance activities of regional collaboration above those identified within the annual budget.

Property Act Fund Reserve

43. This reserve relates to the value of property sold where the Commissioner can retain the income for use in accordance with the Property Act.

Drug Fund

44. This reserve relates to a historical balance in the accounts and is money for initiatives that reduce drug related crime.

Revenue Grants

45. This reserve combines the small amounts of grant income on completed projects where the grant conditions do not require repayment. Cumulatively they create a sizeable reserve. The use of this reserve will be subject to evaluation of any risk of repayment and the submission of a business case.

Animal Welfare Reserve

46. This reserve was established to support the policy for the welfare of animals specifically police dogs on retirement as working animals. There is a panel which meet with representatives from the Vets and the Force and to approve any claims against this fund. Any approved expenditure relating to ongoing welfare as a result of work related injuries can then be paid from this fund.

Tax Base & Transition

47. The timing of data for the production of the Police & Crime budget and precept is such that estimated tax base data will have to be used for the budget and precept report. Actual data from billing authorities is not required to be provided until 31st January. As a result the estimated precept to be collected may vary once the actual data is shown and use of this reserve negates the need to revise the budget breakdown.
48. Despite the recent local reforms to the tax base collection rates have remained high.
49. This reserve will also be used to finance the OPCC's contribution to Single Person Discount Reviews. These reviews are undertaken once every 3-4 years. Where the reviewer successfully identifies that the Single Person Discount is not applicable and the record remains unchanged for 6 months a fee is due to the reviewing company. No fee is paid for unchanged details or where there is a new application within 6 months at that property. This is a jointly commissioned piece of work between Billing Authorities and Precepting Authorities. The benefit is achieved in a higher tax base for the following year and this usually is far more substantial than the initial costs to cover the fees.

Procedure for Use of Reserves

50. The use of reserves requires approval of the Chief Finance Officer to the Commissioner and the Commissioner.
51. All requests should be supported by a business case unless there is an approved process for use, such as the Animal Welfare Reserve.

52. On occasion where an urgent request is being made this should comply with the protocol between the Chief Constable and the Chief Finance Officer to the Commissioner.

Monitoring

53. The level of Reserves is kept under continuous review. The Commissioner receives reports on the levels of reserves as part of the Medium Term Financial Plan updates together with the Annual strategy in January and the out-turn position in June each year.

Risk Analysis

54. Any recommendations that change the planned use of Reserves reported within the Annual Budget and Precept Reports will take account of the need for operational policing balanced against the need to retain prudent levels of Reserves.
55. However, there are significant risks, which affect the level of reserves to be maintained, and it is for this reason that a minimum level of 2% (with a maximum level of 5%) of total net budget has been set for the General Reserve.
56. The significant risks that have been considered, but which will also be kept under review are:
- Current Employment Tribunals relating to A19.
 - The budget monitoring report highlights potential risks in being able to achieve the required efficiencies and savings during 2014-15. This may need to be supplemented by the use of reserves to smooth budget pressure whilst transformational change delivers the savings.
 - The ability to seek financial assistance from the Home Office for major incidents has been diminished and can no longer be relied upon.
 - The need to finance organisational change and redundancies will have an impact on the use of reserves, although this is also reducing in value and risk.
 - The ability to recover significant overspends by divisions and departments would be very difficult in the current financial climate.
 - The instability of the Financial Markets means that the investments we make with balances are currently exposed to greater risk. This is negated by the Treasury Management Strategy, but returns on investment have reduced significantly.

- The grant settlement within the current CSR has been extremely curtailed. There is also an indication of further significant cuts within the next CSR. There remains a gap in funding for the next 3 years and potentially beyond this.
- Should the Commissioner and Force be faced with two or more of the above issues at the same time then the reserves may be needed in full.
- Once utilised there is very little opportunity for reimbursing the level of reserves through precept due to referendum limits or grant, due to the impact it would have operationally.

CFO Opinion

It is my opinion that the current level of reserves whilst healthy are not excessive especially when compared with the averages level of reserves held within all local authorities and within the police and crime sector.

The CLG has published local authority data on levels of reserves as part of the LA Revenue Expenditure and Financing England series. This is shown below and compared with Police & Crime Reserves and Nottinghamshire Police & Crime Reserves.

Type	Highest		NOPCC 2015-16
General Reserves	Met 6%	Average all types of LA 5%	3.7%
Earmarked Reserves	Average all types of LA 16%	Shire OPCC 11%	8.8%

The reserves have grown within the past few years as the force went through a process of change during which time underspends against budget resulted. Tighter budget management means that underspends of this level are not likely; indeed the possibility of over spends against budget becomes a greater risk. This reflected by a reduction in the percentage of reserves held (9.3% previous year).

It will be probable that small levels of overspend will need to use of reserves to finance them. But this is not sustainable and the force will need to work hard to deliver against the programme of efficiencies.

STRATEGY REVIEW

This strategy will be reviewed annually and the Police & Crime Commissioners approval sought.

During the year changes may occur in the MTFP, which affect this strategy. Such changes will be monitored by the Chief Finance Officer and reported to the Commissioner for approval.

Charlotte Radford (CPFA)
Chief Finance Officer

Appendix AReserves Risk Assessment
2015-16GENERAL RESERVE

RISK	IMPACT	PROBABILITY	Min £m	Max £m	Proposed for 2015-16 £m
Major Incident(s) Unbudgeted expenditure	Any amount under 1% of net budget is to be funded by the authority. Amounts over 1% of net budget are subject to Home Office application approval	Single Incident amounting to less than 1% of net budget. Medium Multiple incidents amounting to over 1% of net budget. Medium Single incident amounting to over 1% of net budget. Low	2.1	4.2	4.2
Major Disaster (e.g. natural)	Operation policing affected and resources diverted. (e.g. through building being inaccessible and disaster recovery plan being auctioned)	LOW	0.5	1.0	0.5
Partnership Support	Funding for posts and PCSO's withdrawn. This has also been risk assessed as part of the budget assumptions.	Medium to HIGH	0.5	4.6	1.2
Counterparty failure	If invested balances were tied up in a process to recovery there would be an immediate impact on the revenue budget (possibly short term).	LOW	0.5	5.0	0.5
Employment Tribunals and other litigation	Direct impact on revenue budgets	LOW (A19 will be met from the MTFP Reserve)	0.1	0.5	0.1
Insurance	Emerging Risks and late reported claims	To date no claims of this type have affected the accounts. Low to MEDIUM	0.3	0.7	0.5
TOTAL					7.0

Earmarked Reserves Assessment

RISK/RESERVE	PURPOSE	HOW AND WHEN IT WILL BE USED	Management and control	Review	Estimated Balance at 31.03.15 £m
Medium Term Financial Plan (MTFP)	To provide against financial shortfalls identified within the MTFP	Smoothing peaks and troughs in financing the MTFP	Chief Finance Officer & Commissioner	Minimum twice annually	11.184
PCC Transition	To cover cost associated with PCC transition and Stage 2 transition	During the year cost will be charged to a separate cost centre and will be charged to the reserve at year end.	Chief Finance Officer	Ongoing	0.405
Grants & Commissioning	To collate small balances within revenue accounts to provide funding for this growing area of work.	To meet specific requirements relating to Grants and Commissioning.	Chief Finance Officer	Ongoing	0.283
PFI reserve	To fund PFI related expenditure	Extraordinary event relating to the contract	Chief Finance Officer	Annually	0.258
JCO – Jointly Controlled Operations	To provide for unexpected expenditure relating to regional collaboration.	Decisions relating to the use of this fund follow the regional governance arrangements.	EM meeting of the PCC's.	Annually	0.948

Property Act Fund	Income from the sale of property act confiscations	To be determined by the Police & Crime Commissioner	PCC and CFO	Annually	0.106
Drug Fund	For use in reducing drug related crime	To be determined by the Police & Crime Commissioner	PCC and CFO	Annually	0.064
Revenue Grants	Balances on grants not required to be repaid	To be determined by the Police & Crime Commissioner	PCC and CFO	Annually	2.954
Animal Welfare	To set up a scheme for animal welfare on retirement as working animals	Scheme to be established in 2013-14	Set up November 2012.	During the year	0.020
Tax Base	To iron out fluctuations caused between estimated and actual tax base data. Also to assist with risk relating to the removal of redistributed business rates in future years.	Annually to balance the budget. Every 3-4 years to finance Single Person Discount Review	Chief Finance Officer	Annually	0.230 TBC
TOTAL					16.452

Tables to show the use of General Reserves

	2015-16			2016-17			2017-18			2018-19		
	01.04.15 balance £m	Use in year £m	01.04.16 balance £m	01.04.16 balance £m	Use in year £m	01.04.17 balance £m	01.04.17 balance £m	Use in year £m	01.04.18 balance £m	01.04.18 balance £m	Use in year £m	01.04.19 balance £m
General Reserve	7.000	0	7.000	7.000	0	7.000	7.000	0	7.000	7.000	0	7.000
EMSOU general reserve	0.074		0.074	0.074		0.074	0.074		0.074	0.074		0.074
<i>% of net budget</i>	3.7%			3.8%			3.9%			4.0%		

Tables to show the use of Earmarked Reserves

	2015-16			2016-17			2017-18			2018-19		
<u>Earmarked Reserves</u>	01.04.15 balance £m	Use in year £m	01.04.16 balance £m	01.04.16 balance £m	Use in year £m	01.04.17 balance £m	01.04.17 balance £m	Use in year £m	01.04.18 balance £m	01.04.18 balance £m	Use in year £m	01.04.19 balance £m
MTFP	11.184	(3.000) +3.000	11.184	11.184	(1.000) +3.000	13.184	13.184	(0.002) +1.000	14.182	14.182	TBC	14.182
PCC Transition	0.405	(0.405)	0									
Grants & Commissioning	0.283	(0.043)	0.240	0.240		0.240	0.240		0.240	0.240		0.240
PFI	0.258	0.036	0.294	0.294	0.036	0.330	0.330	0.036	0.366	0.366	0.036	0.402
JCO	0.948		0.948	0.948		0.948	0.948		0.948	0.948		0.948
Property Act Fund	0.106		0.106	0.106		0.106	0.106		0.106	0.106		0.106
Drug Fund	0.064		0.064	0.064		0.064	0.064		0.064	0.064		0.064
Revenue Grants	2.954		2.954	2.954		2.954	2.954		2.954	2.954		2.954
Animal welfare	0.020	(0.001)	0.019	0.019	(0.001)	0.018	0.018	0.002	0.020	0.020	(0.001)	0.019
Tax Base	0.230		0.230	0.230		0.230	0.230		0.230	0.230		0.230
TOTAL	16.452	(0.413)	16.039	16.039	2.035	18.074	18.074	1.036	19.110	19.110	0.035	19.145

Please note at the time of this review there were gaps in balancing the budget for 2016-17, 2017-18 and 2018-19. These gaps may require use of the MTFP Reserve in order to set a balanced budget.