



**NOTTINGHAMSHIRE
POLICE AUTHORITY**

Nottinghamshire Police Authority

Reserves Strategy 2012-13

Reserves Strategy 2012-13

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 authorities over-committing themselves financially. These include:
 - The balanced budget requirement (local government Act 1992 s32 and s43).
 - Chief Finance Officers (Treasurer) duty to report on the robustness of estimates and adequacy of reserves (Local Government Act 2003 s25) when the authority is considering its budget requirement.
 - Legislative requirement for each authority 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 all of the authority's members 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 authority 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 full authority must meet within 21 days to consider the s114 notice and during that period the authority is prohibited from entering into new agreements involving the incurring of expenditure. *In this context, this includes the Force in the definition of authority.*

5. Whilst it is primarily the responsibility of the authority and its chief financial 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 authorities or authorities in general.
6. CIPFA's Prudential Code requires the chief finance officers in authorities to have full regard to affordability when making recommendations about the authority's future capital programme. Such consideration includes the level of long-term revenue commitments. Indeed, in considering the affordability of its capital plans, the authority 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 all authorities and this is achieved through the Medium Term Financial Plan (MTFP). The Comprehensive Spending Review (CSR) has provided the Authority details of proposed grant settlement for two years and an indication of what years 3 and 4 might be. This provides ability to focus on the levels of reserves and application of authority 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. Authorities 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 authorities. A well-managed authority, 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 authority 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 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 over the next few years are intense. Therefore, the ability to retain reserves for unforeseen events and circumstances becomes not only difficult, but something that requires careful consideration.
10. Members will also need to consider any requirement for additional reserves to finance the organisational changes required over the next few years (eg redundancy costs). An estimate of redundancy costs for 2012-13 has been included within the strategy; once more accurate information becomes available it will be possible to assess future requirements for such purposes.

Types of Reserve

11. When reviewing the medium term financial plans and preparing the annual budgets authorities 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 Authority's financial assets. This would link closely with the Authority's Treasury Management and Prudential Code Strategy.
12. Authorities also hold other reserves that arise out of the interaction of legislation and proper accounting practice. These reserves, which 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.

13. 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.

14. In addition authorities 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.

15. For each earmarked reserve held by the authority 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

16. When establishing reserves, authorities need to ensure that they are complying with the Code of Practice on Local Authority Accounting and in particular the need to distinguish between reserves and provisions.

Nottinghamshire Police Authority Reserves

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

The General Reserve

18. It has previously been agreed by the Authority that General Reserves will be maintained at a level above the minimum of 2.0% of the total net budget.

19. 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.

20. 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 for the Authority is 5.0% of the total net budget.

21. Authorisation to finance such expenditure must be obtained in advance from the Treasurer in accordance with the scheme of delegation and the protocol between the Chief Constable and the Treasurer.

22. As the net budget position changes the level of General Reserve must be monitored to ensure the minimum level is maintained. This is particularly relevant where revenue carry forwards are identified as part of the year-end process.

23. **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.

Earmarked Reserves

24. 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 authority to identify such areas of expenditure and set aside amounts that limit future risk exposure.

25. Such expenditure usually arises out of changes in policy (for example MTFP) or where the Authority is working in collaboration with other forces to provide a specific service (for example Air Support Unit).

26. Expenditure relating to earmarked reserves has to specifically relate to the purpose of the reserve.

27. **Appendix B** details each of the earmarked reserves that existed at the start of the 2011-12 financial year and their estimated balance by 31st March 2012. Details of those available for use in 2012-13 are given below:

Medium Term Financial Plan (MTPF) Reserve

28. The medium term financial plan of the Authority is under constant review and changes as new and more information becomes available.

29. The original purpose of this reserve is to alleviate financial pressure on the budgets in future years. ***It is proposed that the Air Support Unit Reserve is transferred to the MTFP Reserve once the Unit transfers to the National Air Support Service.***

30. The support from this reserve is only one-off support and as such cannot be used to finance ongoing commitments.

31. 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 organisational changes over the next few years. A specific MTPF Provision has also been created for the costs associated with redundancy from the organisational restructure and to smooth budget pressures as they arise.

32. In line with revised plans for 2011-12 it is intended that budget savings from the 2011-12 financial year will be added to this reserve.

33. The Medium Term Financial Plan has a risk assessment in relation to achieving the efficiencies identified. As such this reserve would be the first call for balancing the accounts should the efficiencies not be realised.

34. **Appendix C** shows how the remainder of this reserve has been initially allocated to support the cost of change over the next four years.

Air Support Operational Reserve

35. Nottinghamshire and Derbyshire operate a joint Air Support service. This reserve is to cover unexpected expenditure specifically relating to this joint service. The amount shown within the reserves tables in Appendix B and C is the portion of the reserve specifically relating to Nottinghamshire.

36. With the Air Support Unit transferring to the National Air Support Service (NPAS) there will no longer be a need to maintain this reserve and therefore it will transfer to the MTFP reserve.

Carry Forwards

37. This is classified as a reserve for accounting purposes, but actually represents underspent budget of the previous year. For 2011-12 no underspends were carried forward by departments. In light of the financial difficulties underspends are currently being transferred to reserves for strategic use.

38. It would not be prudent to allow underspends to be carried forward and in exceptional circumstances not all overspends are carried forward. Overspends by their nature are not reserves.

East Midlands Special operations Unit (EMSOU) Reserve

39. The Authority works collaboratively with the other four regional Police Authorities in providing this specialised unit of policing.

40. There is an EMSOU Board, which makes decisions on Policing activity, and this reports to the East Midlands Joint Police Authorities Committee (EMJPAC).

41. The reserve exists to finance activities of the unit above those identified within the annual budget.

Monitoring

42. The level of Reserves is kept under continuous review. Members receive reports on the levels of reserves as part of the Medium Term Financial Plan updates (at Members Business Meetings and Police Authority Meetings).

Risk Analysis

43. 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.

44. 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.

45. The significant risks that have been considered, but which will also be kept under review are:

- 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 a significant impact on the use of reserves.
- The ability to recover significant overspends by divisions and departments is becoming 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.
- The grant settlement within the current CSR has been extremely curtailed. There is also a proposed mid-term CSR to assess how effective the current measures in addressing the National debt have been. This review could see further cuts in public sector expenditure in the future.
- Should the Authority 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.

STRATEGY REVIEW

This strategy will be reviewed annually and Members approval sought.

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

Charlotte Radford (CPFA)
Deputy Chief Executive & Treasurer

Reserves Risk Assessment

2012-13

GENERAL RESERVE

RISK	IMPACT	PROBABILITY	Min £m	Max £m	Proposed for 2011-12 £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. HIGH 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 (eg natural)	Operation policing affected and resources diverted. (eg 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	0.1	0.5	0.1
Insurance	Emerging Risks and late reported claims	To date no claims of this type have affected the Authority's accounts. Low to MEDIUM	0.3	0.7	0.5
TOTAL					7.0

Appendix B**Earmarked Reserves Assessment**

RISK/RESERVE	PURPOSE	HOW AND WHEN IT WILL BE USED	Management and control	Review	Estimated Balance at 31.03.12 £000
Medium Term Financial Plan (MTFP)	To provide against financial shortfalls identified within the MTFP		01.04.09 £9.143m	Minimum twice annually	6,637
Air Support Unit Operational reserve	To provide for unexpected expenditure relating to the jointly owned helicopter with Derbyshire.	North Midlands Helicopter Joint Members Panel would identify and agree the use of this reserve.	The North Midlands Helicopter Joint Members Panel 01.04.09 £90k	Annually	90
Carry forwards	Previously underspends of up to 0.75% could be carried forward to the following financial year.	Requires Authority approval.	01.04.09 £910k 01.04.10 £0	Annually	0
PFI reserve	To fund PFI related expenditure	Extraordinary event relating to the contract		Annually	271
EMSOU	To provide for unexpected expenditure relating to the EMSOU operation	The EMSOU board and East Midlands Joint Committee will authorise how and when this reserve is to be used.	EMSOU board, Joint committee and reports to the regional Finance Directors and Treasurers.	Annually	189
TOTAL					7,187

Tables to show the use of Reserves

	2012-13			2013-14			2014-15			2015-16		
	01.04.11 balance £m	Use in year £m	01.04.12 balance £m	01.04.12 balance £m	Use in year £m	01.04.13 balance £m	01.04.13 balance £m	Use in year £m	01.04.14 balance £m	01.04.14 balance £m	Use in year £m	01.04.15 balance £m
General Reserve	7.0	0	7.0	7.0	0	7.0	7.0	0	7.0	7.0	0	7.0
<i>% of net budget</i>	3.49%			3.62%			3.67%			3.69%		

Earmarked Reserves

	2012-13			2013-14			2014-15			2015-16		
	01.04.12 balance £m	Use in year £m	01.04.13 balance £m	01.04.13 balance £m	Use in year £m	01.04.14 balance £m	01.04.14 balance £m	Use in year £m	01.04.15 balance £m	01.04.15 balance £m	Use in year £m	01.04.16 balance £m
MTFP	6.637	(3.210)	3.427	3.427		3.427	3.427		3.427	3.427		3.427
Air Support	0.090	(0.090)	0	0								
PFI	0.271		0.271	0.271		0.271	0.271		0.271	0.271		0.271
EMSOU	0.189		0.189	0.189		0.189	0.189		0.189	0.189		0.189
TOTAL	7,187	(3.300)	3.887	3.887	0	3.887	3.887	0	3.887	3.887	0	3.887