Buckinghamshire & Milton Keynes Fire Authority

MEETING	Executive Committee
DATE OF MEETING	18 November 2015
OFFICER	David Sutherland, Acting Director of Finance & Assets
LEAD MEMBER	Councillor Andy Dransfield
SUBJECT OF THE REPORT	**Realignment of Reserve Balances to Facilitate the Medium Term Financial Plan**
EXECUTIVE SUMMARY	Over a number of years the Authority has built up substantial balances within its usable reserves. This paper evaluates the on-going requirement for each reserve currently held. The total usable reserves as at 31 March 2015 were **£15.9m**. It is essential however that the level of reserves is considered in the context of other assets and liabilities, with particular regard given to the capital financing requirement (CFR). The CFR measures the Authority's underlying need to borrow (or finance by other long-term liabilities) for a capital purpose. It represents the amount of capital expenditure that has not yet been resourced. The underlying CFR (excluding the finance lease) as at 31 March 2015 was **£6.5m**. In order to finance this the Authority is required to make a minimum revenue provision (MRP) each year. The MRP budget (excluding finance lease) for 2015/16 is **£0.25m**. It is recommended that usable reserves are realigned and that the balances not immediately required are used to make a voluntary revenue provision to reduce the CFR (excluding finance lease) down to zero. The advantages of this include: • The authority will no longer be required to make a MRP each year and can instead use this amount to finance the capital programme, as the Authority no longer receives an automatic entitlement to capital grant funding. This will support the Property and Fleet strategies. • It provides clarity and transparency regarding the remaining reserve balances and better represents the true financial position of the Authority. • No cash is repaid, so investment interest will be unaffected (currently the repayment premiums effectively prohibit early repayment of debt). The latest MTFP for revenue and capital are shown in

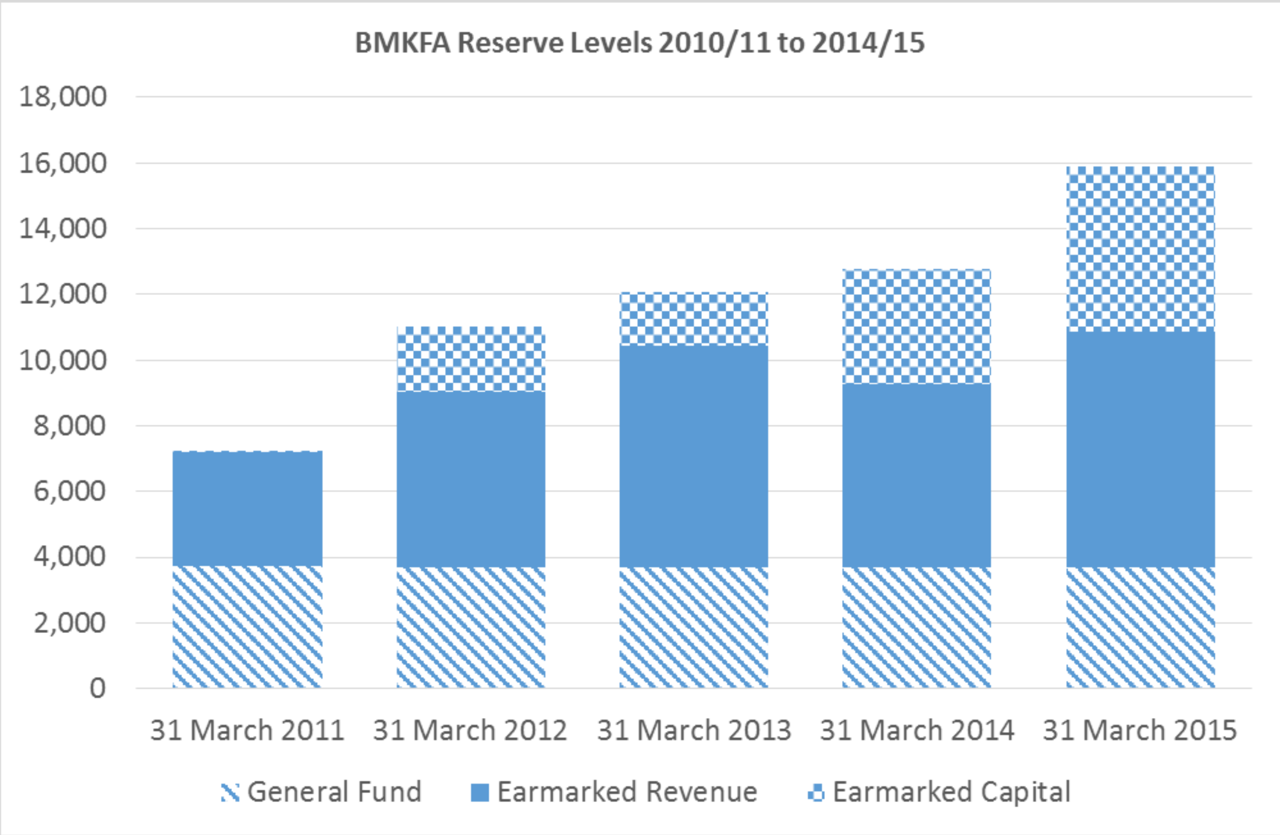
	Appendices D and E respectively. It should be noted that these are still subject to further officer and Member challenge. The Authority is still also awaiting the outcome of the Comprehensive Spending Review and settlement (expected November/December 2015) and Council Tax and Business Rate funding levels will be confirmed by the billing authorities in January 2016. These two models are built on revised assumptions, the principal ones being that the Authority will hold Council Tax at the current level and accept the 1% Council Tax Freeze Grant every year (if available) and that the Council Tax base will increase by 2% per annum. The models demonstrate that reallocating the reserves as recommended still provides the Authority with sufficient reassurance that the remaining levels are adequate to support the MTFP, and that the Authority's financial position remains solid.
ACTION	Decision
RECOMMENDATIONS	It is recommended that: 1. the proposed reallocation between reserves detailed in Appendix B be approved; 2. the use of usable reserves to reduce the capital financing requirement (excluding finance lease) to zero (as shown in Appendix B) be approved.
RISK MANAGEMENT	The recommended risk assessed General Fund balance is detailed in Appendix B. The risk of usable reserves being insufficient is mitigated by being able to increase the CFR in future if required. As part of its risk management, the Authority also holds a corporate contingency within the budget. The contingency budget for 2015/16 was set at £1.3m. It is anticipated this will be reduced to £0.6m as part of the MTFP.
FINANCIAL IMPLICATIONS	The key implications are: • Usable reserves would decrease by £6.3m. • The capital financing requirement would reduce by the same amount. • The MRP charge of £0.25m in the budget for 2016/17 would be reallocated to revenue contribution to capital to ensure the on-going sustainability of the capital programme. The projected level of this contribution for 2016/17 would be £2.2m.

LEGAL IMPLICATIONS	Section 42A of the Local Government Finance Act 1992 and Section 25 of the Local Government Act 2003 require the Authority to have regard to the level of reserves needed for meeting estimated future expenditure when calculating the budget requirement and to reports of the chief finance officer on the robustness of budget estimates and the adequacy of reserves.
CONSISTENCY WITH THE PRINCIPLES OF COLLABORATION	No direct impact.
HEALTH AND SAFETY	No direct impact.
EQUALITY AND DIVERSITY	No direct impact.
USE OF RESOURCES	See Financial Implications.
PROVENANCE SECTION & BACKGROUND PAPERS	LAAP Bulletin 99 – Local Authority Reserves and Balances, CIPFA, July 2014: http://www.cipfa.org/~/media/files/policy%20and%20guidance/laap%20bulletins/laap99%20reserves%20and%20balances.pdf?la=en
APPENDICES	Appendix A – Historic and Comparative Reserve Balances Appendix B – Recommended Reserve Movements Appendix C – Explaining the CFR and MRP Appendix D – Current Revenue MTFP Appendix E – Current Capital MTFP
TIME REQUIRED	15 minutes.
REPORT ORIGINATOR AND CONTACT	David Sutherland dsutherland@bucksfire.gov.uk 01296 744662

Appendix A – Historic and Comparative Reserve Balances

Historic Reserve Levels

The chart below shows the level of usable reserves for the previous five financial years:



The total usable reserves of the Authority have more than doubled over the preceding five years, despite large cuts to the cost of service over the same period.

Reserves are an essential part of good financial management. They allow authorities to manage unpredictable financial pressures and plan for their future spending. The level, purpose and planned use of reserves are important factors for Members to consider in developing medium-term financial plans (MTFP) and setting annual budgets. Reserves are held for three main purposes:

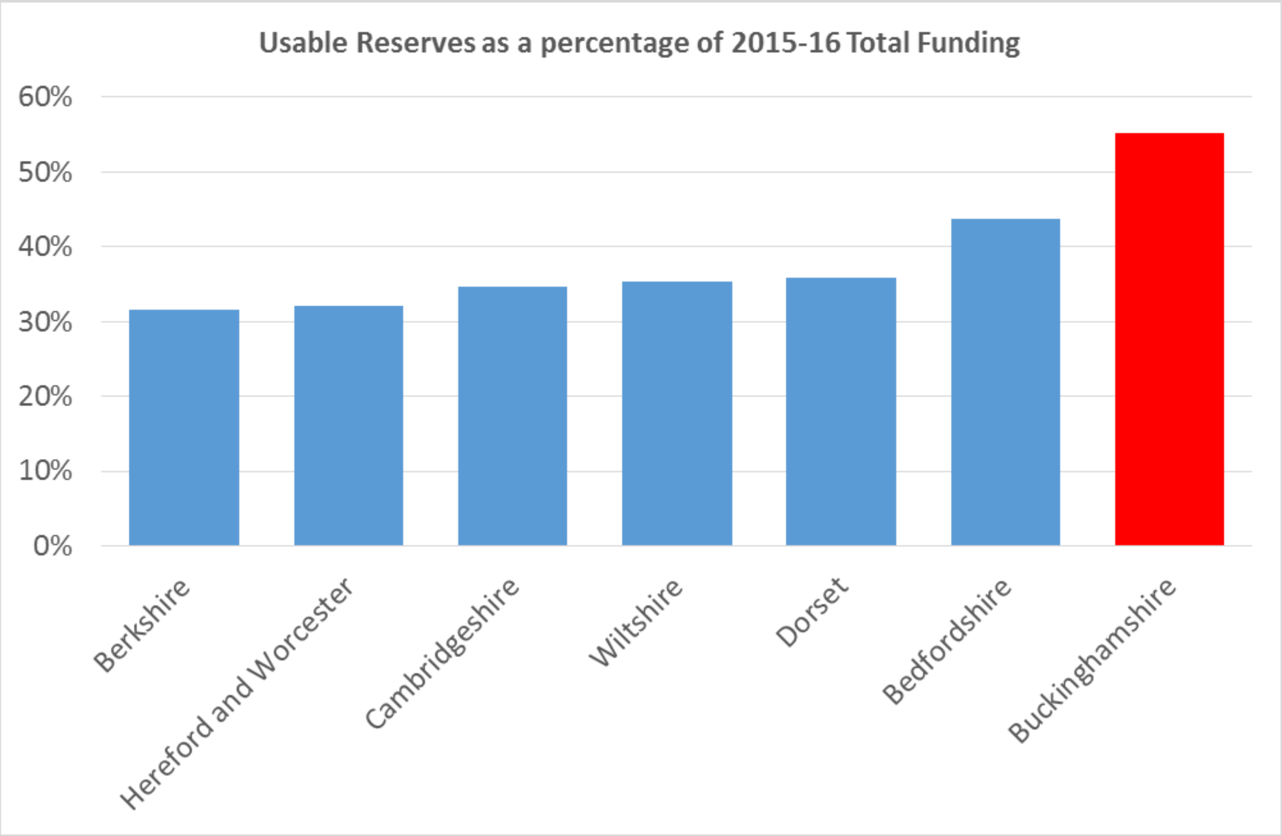
- a working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – this forms part of general reserves
- a contingency to cushion the impact of unexpected events or emergencies – this also forms part of general reserves
- a means of building up funds (often referred to as earmarked reserves) to meet known or predicted requirements

Within the existing statutory and regulatory framework, it is the responsibility of the chief finance officer to advise the Authority about the level of reserves that it should hold and to ensure that there are clear protocols for their establishment and use.

Level of Reserves Compared to Other Combined Fire Authorities

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 local authorities. However, the government has undertaken to apply this only to individual authorities in the circumstances where an authority does not act prudently, disregards the advice of its chief finance officer and is heading for serious financial difficulty.

It is useful however to look at the level of reserves held by authorities facing similar circumstances. The chart below shows the level of usable reserves as at 31 March 2015 as a percentage of total funding for 2015/16, compared to other local and/or similar sized combined fire authorities:



This shows that the level of usable reserves held by the Authority as a percentage of budget is far in excess of the level of comparable authorities.

Given the Authority's excellent record of planning and pro-active management of expenditure, it should have the capacity to reduce the level of reserves significantly.

Appendix B – Recommended Reserve Movements

Section 1 - Usable Reserves

The reserve balances as at 31 March 2015 are shown in the table below, along with commentary on the recommended treatment.

Reserve	Balance at 31 March 2015	Projected Transfers In/Out 2015/16	Committed to Capital Schemes	Proposed Reallocation	Projected Residual Balance	Recommendation
General Fund Balance	(3,700)	(1,657)	-	3,357	(2,000)	Reduce to £2m as per revised risk assessed level (see Appendix B – Section 2).
Sub Total General Fund Balance	**(3,700)**	**(1,657)**	**-**	**3,357**	**(2,000)**	
Fire Control Reserve	(150)	150	-	-	-	This reserve is required to cover costs incurred in the early part of 2015/16.
Invest to Save Reserve	(500)	-	-	250	(250)	Recommend this is retained but reduced to £250k to help fund one-off cost of change within the Public Safety Plan.
New Dimensions Reserve	(1,000)	-	-	1,000	-	This was originally setup to provide protection if section 31 grant funding was to cease. This is now covered within the General Fund risk assessed level so this can be used for other purposes.
Redundancy and Early Retirement Reserve	(477)	-	-	227	(250)	Recommend this is retained but reduced to £250k to help fund staff change initiatives within the Public Safety Plan.
Vehicle Reserve	(191)	-	-	191	-	Recommend this is transferred to the Revenue Contribution to Capital Reserve.
Funding Pressures Reserve	(1,277)	87	-	1,190	-	A small amount of this is required to fund 2015/16 pressures identified in 2014/15. All general funding pressures are now covered within the General Fund risk assessed level so the remainder can be used for other purposes.
Control Room Reserve (Revenue)	(1,360)	204	-	1,156	-	Thames Valley Fire Control is now live. A small amount will be required in 2015/16, but any residual balance should be used for other purposes.

Reserve	Balance at 31 March 2015	Projected Transfers In/Out 2015/16	Committed to Capital Schemes	Proposed Reallocation	Projected Residual Balance	Recommendation
RDS Pension Contributions Reserve	(650)	-	-	650	-	This reserve was originally setup to pay back-dated employer contributions to the Modified pension scheme. However, it is now anticipated that contributions will be set as part of the scheme valuation, rather than requiring a lump sum contribution. This reserve can therefore be utilised for other purposes.
Continuing Projects Reserve	(1,500)	-	-	300	(1,200)	£300k of this relates to Thames Valley Fire Control, which is now live and that amount should be used for other purposes. The remaining £1.2m relates to the systems integration project, and the full amount of this is still required.
Insurance Reserve	(50)	-	-	-	(50)	This reserve is to offset the cost of the insurance excess should there be an unusually large number of claims in any one year. It is recommended this amount is retained in full.
Sub Total Earmarked Reserves - Revenue	**(7,155)**	**441**	**-**	**4,964**	**(1,750)**	
Usable Capital Receipts Reserve	(93)	-	93	-	-	This reserve is mandatory, as receipts generated from the sale of assets can only be used to finance capital expenditure.
Control Room Capital Grant Unapplied	(800)	-	800	-	-	This reserve will be fully utilised during 2015/16.
Other Capital Grants Unapplied	(86)	(3,240)	3,326	-	-	This reserve is mandatory and reflects the timing difference between the receipt of one-off capital grants and the capital expenditure to which they relate.

Reserve	Balance at 31 March 2015	Projected Transfers In/Out 2015/16	Committed to Capital Schemes	Proposed Reallocation	Projected Residual Balance	Recommendation
Revenue Contribution to Capital	(4,052)	(2,153)	4,839	(2,065)	(3,431)	This reserve holds contributions from the revenue budget towards the capital programme. Since there is no longer an automatic entitlement to capital grant this reserve is required, and will continue to be topped-up by an amount from revenue each year. The balance of other reserves not required to reduce the CFR is to be allocated here to support the fleet and property strategies.
Sub Total Earmarked Reserves - Capital	**(5,031)**	**(5,393)**	**9,058**	**(2,065)**	**(3,431)**	
Total	**(15,886)**	**(6,609)**	**9,058**	**6,256**	**(7,181)**	

Capital Financing Requirement	8,346	(311)	-	(6,256)	1,779	The proposed reallocation from usable reserves will reduce the CFR (excluding finance lease) to zero. The residual balance will be reduced over the remaining lease term as payments are made).

It should be noted that the projected residual balance will almost certainly be different from the actual balance as at 31 March 2016 for the General Fund and the capital reserves. The balance on the General Fund will depend on the exact revenue outturn figure, which may change from the current projection. The balance across the capital reserves will depend on the capital outturn, particularly the timing of major schemes. The residual balance across capital reserves is intended to show the available reserves once all schemes in the 2015/16 capital programme have been completed. This residual balance represents the amount available to fund future schemes.

The projected residual balance for all reserves would represent 25% of the Authority's 2015/16 funding (based on the reserve balances as at 31 March 2015 this percentage is 55%). This is much more in line with other similar authorities and the Authority's excellent record of managing expenditure and savings and risk.

Section 2 - Recommended Risk Assessed General Fund Balance

In order to assess the adequacy of unallocated general reserves when setting the budget, chief finance officers should take account of the strategic, operational and financial risks facing the authority. The assessment of risks should include external risks, such as flooding, as well as internal risks, for example, the ability to deliver planned efficiency savings. The following table sets out the key risks taken into account when assessing the required level of the General Fund:

Risk description	**Risk factor - likelihood Rank % factor {a}**	**Risk factor - impact Rank % factor {b}**	**Potential Amount Required £000 {c}**	**Assessed Risk £000 {a} x {b} x {c}**
Savings assumptions - The savings built into the MTFP are dependent on a number of factors and reliant on estimates made.	25%	100%	2,268	567
Capital budget assumptions - buildings. Limited capacity built into the budgets for unseen events. Current value of buildings is £16.3m.	5%	50%	16,337	408
Funding – there is a risk that the funding received is less than forecast within the MTFP.	20%	5%	28,246	282
Property - limited provision for capital maintenance. Would need to resort to use of reserves.	25%	100%	1,000	250
Public risks - there is no provision in the budgets for injury or damage to public or public property if the organisation is found to be negligent in its duty of care.	1%	100%	10,000	100
Pay awards - budget includes 1% increase. This could vary dependent on national agreements	50%	80%	213	85
Legal fees - there are times when it is necessary to take cases through the courts. There is provision in the budgets for this. However, there is always a risk that fees become burdensome and the case is lost with loss of our fees and the possibility that we would need to fund the claimant's costs	20%	75%	500	75
Thames Valley Fire Control project - potential issues post cut-over	25%	20%	1,500	75

Spate conditions - the budget is set on the assumption that there is a normal pattern of turnouts for whole time and on-call staff. In the event of extraordinary circumstances where turnouts significantly exceed the norm and overtime runs above the normal allowance, there would be an impact on reserves.	20%	70%	500	70
Vehicles - risk of losses not covered by insurance policies. No provision within the budgets so would need to be covered from reserves	10%	20%	3,199	64
Staff risks - injury payments for uninsured risk - i.e. the organisation is found to be negligent in its duty of care to staff	10%	100%	500	50
Local Government Pension Scheme - triennial revaluation may increase employer costs	15%	25%	473	18
Inflation budget assumptions - especially fuel and utilities	10%	50%	90	5
General Fund Balance Requirement				**2,049**

Reserve Protocols

The protocols for the remaining reserves are set out in the table below:

Reserve	**Reason/Purpose**	**How and When Reserve Can be Used**
General Fund Balance	Mandatory reserve to hold all non-earmarked reserve balances.	This will be used/added to at year-end depending on the revenue outturn
Invest to Save Reserve	To help fund one-off cost of change for projects detailed within the Public Safety Plan.	As required. Use will require the prior approval of the Executive Committee and production of the relevant business case.
Redundancy and Early Retirement Reserve	To help fund one-off cost of staff changes to facilitate the Public Safety Plan.	As required. Use will require the prior approval of the Executive Committee and production of the relevant business case.

Reserve	**Reason/Purpose**	**How and When Reserve Can be Used**
Continuing Projects Reserve	To fund the business and systems integration (BASI) programme approved by the Executive Committee in July 2015.	As required. Only for purposes as set out within the approved business case.
Usable Capital Receipts Reserve	Mandatory reserve to hold receipts from the sale of non-current (fixed) assets.	At year end for financing the capital programme.
Other Capital Grants Unapplied	Mandatory reserve to hold one-off capital grants received but not yet spent.	At year end for financing the capital programme.
Revenue Contribution to Capital	Discretionary reserve to hold revenue contributions used to finance the capital programme.	At year end for financing the capital programme. Can be used in-year for non-capital purposes if required but only with the prior approval of the Executive Committee.

All reserves are controlled and monitored by the Finance team and will be reported to Members quarterly within budget monitoring and annually within the Statement of Accounts. The on-going need for each reserve will be reviewed at least annually as part of the MTFP.

Appendix C – Explaining the Capital Financing Requirement (CFR) and Minimum Revenue Provision (MRP)

The CFR measures the Authority's underlying need to borrow (or finance by other long-term liabilities) for a capital purpose. It represents the amount of capital expenditure that has not yet been resourced. Minimum revenue provision (MRP) is the amount set aside from the revenue budget each year to ensure that the Authority is able to repay the debt when it falls due.

An example of the interaction between borrowing, the CFR and MRP is shown below to aid understanding of this paper.

<u>Example</u>

Authority A borrows £1m that is repayable on maturity. They use it to purchase a number of large vehicles with asset lives of 10 years.

In the first year, the Authority has incurred a liability of £1m (the amount it has borrowed) and has a number of assets worth £1m.

Every year, the assets will be depreciated and at the end of the 10 year period will be worth nothing. However, the liability has not decreased as only the interest has been paid each year. In this situation Authority A would have to borrow a further £1m in order to repay the initial liability (and this would continue indefinitely if nothing else changed).

To avoid this situation, authorities are required to set aside an amount from revenue each year to repay borrowing. This is known as the MRP. In this example, the MRP each year would be £100k, so that at the end of the 10 year period, £1m has been set aside (i.e. £100k x 10 years). MRP is not a cash payment out, but is a notional charge against the general fund that effectively 'ties up' the cash so that it cannot be spent on anything else.

The MRP in relation to finance leases is calculated on a different basis. The MRP relating to assets held under by the Authority a finance lease will continue to be set aside on an annual basis as per the current situation.

Appendix D – Current Revenue MTFP

	2015/16 £000	2016/17 £000	2017/18 £000	2018/19 £000	2019/20 £000
Base Budget	27,499	28,740	28,374	28,346	27,779
Pay Adjustment	213	565	222	224	204
Inflation Adjustment	88	90	103	88	86
Savings	-1,096	-559	0	0	0
Growth	728	1,247	-99	-193	5
Previous year savings & growth adjustments	-888	-824	-254	-686	0
Contingency	1,309	-669	0	0	0
Revenue Contribution to Capital	887	-216	0	0	0
Net Budget Requirement	**28,740**	**28,374**	**28,346**	**27,779**	**28,074**
Government Funding	-5,170	-4,009	-2,888	-2,232	-1,508
Business Rates	-5,158	-5,380	-5,535	-5,692	-5,855
Council Tax Receipts Surplus/Deficit	-329	-329	0	0	0
Council Tax Freeze Grant	-182	-173	-292	-387	-397
Specific Grants (S.31)	-1,099	-1,099	-1,099	-1,099	-1,099
Council Tax Receipts	-16,802	-17,256	-17,601	-17,953	-18,312
Total Funding Available	**-28,740**	**-28,246**	**-27,415**	**-27,363**	**-27,171**
Shortfall for year	0	128	931	416	903
Cumulative savings requirement	0	128	1,059	1,475	2,378

Appendix E – Current Capital MTFP

	2015/16 £000	2016/17 £000	2017/18 £000	2018/19 £000	2019/20 £000
Finance and Assets					
Property Capital Expenditure 2016 -17	500				
Finance and Assets Total	**500**	**0**	**0**	**0**	**0**
Delivery, Corporate Development & Planning					
CCTV Cameras	45				
Red Fleet Replacement	2,300	500	500	500	500
Digital Radios					
Battery Powered hydraulic equipment	56	56	56	56	56
Operational Equipment	83	83			
Technical Rescue - Bariatric and Trench Rescue	10	2	2	7	2
Total Delivery, Corporate Development & Planning	**2,494**	**641**	**558**	**563**	**558**
Knowledge and Information Systems					
Wireless Network	35	12	12	12	12
Rolling Replacement of ICT hardware	75	75	75	75	75
Knowledge and Information Systems Total	**110**	**87**	**87**	**87**	**87**
Total Spend	**3,104**	**728**	**645**	**650**	**645**