



Title: **Review of Reserves 2013/14**

Wards Affected: **All Wards in Torbay**

To: **Priorities & Resources Panel** On **30th November 2012**

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**1. What we are trying to achieve and the impact on our customers**

1.1 The Council holds a number of reserves as part of its approach to prudent resource management. These reserves are applied to both specific and general purposes for the benefit of the communities of the Bay. The application and use of the reserves supports the achievement of service delivery and improvements in the Bay, as outlined in the Community and Corporate plans and related strategies.

**2. Recommendations**

2.1 That Council approve the transfer of the surplus of £1.4m identified on a number of individual reserves to the Comprehensive Spending Review Reserve.

**3. Key points and reasons for recommendations**

3.1 A Review of Reserves is a key part of the Council's budget setting process. Consideration of reserve levels is linked to legislation for budget setting contained in both the Local Government Act 2003 and the Localism Act 2011.

3.2 As a result of the increasing risk from the financial pressures facing the Council, in particular from social care and the requirement for ongoing significant budget reductions, on achieving a balanced revenue budget it is recommended that the surplus on a number of reserves, of approximately £1.4m identified, is transferred to the Comprehensive Spending Review Reserve.

**For more detailed information on this proposal please refer to the supporting information attached.**

Paul Looby  
Chief Finance Officer

## A1. Introduction

A1.1 The background as to the Council's responsibilities in relation to its reserves and the Council's current reserve policies are in appendix two to this report.

## A2 Review of Reserves 2013/14

### A2.1 Overview

A2.2 As at 31/03/2012 Torbay Council's reserves were as follows:-

31/3/11		31/3/12	31/3/13 est.	Change
£m		£m	£m	£m
4.0	General Fund Reserve	4.0	4.0	0
5.3	Uncommitted Reserves	3.6	3.4	(0.2)
14.9	Timing of Spend Reserves	15.4	8.9	(6.5)
2.8	Partner/Ring Fenced Reserves	3.6	2.6	(1.0)
2.5	School Reserves	3.5	3.0	(0.5)
9.1	Specific Reserves	10.4	6.2	(4.2)
<b>38.6</b>	<b>Total Reserves</b>	<b>40.5</b>	<b>28.1</b>	<b>(12.4)</b>

A2.3 A list of the Council's Reserves as at 31/03/2012 is attached at Appendix 1.

A2.4 The table in A2.2 shows that the total reserves held by the Council increased by 5% during 2011/12 with over 50% of that increase in schools' reserves. The General Fund Reserve remained at £4.0 million during the same period. This is discussed in more detail below.

A2.5 Each reserve has been assessed by the Service Manager and their finance manager for its estimated balance as at 31<sup>st</sup> March 2013 and for the estimated additions or withdrawals from the reserve during 2013/14 and future years. This is included in the table at Appendix 1. This table is shown after the recommendations arising from this report.

A2.6 The table in A2.2, (based on the review of reserves), shows that the level of reserves is expected to decrease during 2012/13 to £28.1m. The actual balance at year end will depend on spend during the year and any year end service carry forwards from unspent revenue funds and/or unspent grant allocations.

A2.7 More information on all Council Reserves is available that shows details about each reserve, including the reason/purpose of the reserve, how and when the reserve can be used and the process for retention of each reserve to ensure continuing relevance and adequacy.

A2.8 The CIPFA guidance on Reserves and Balances (LAAP 77 issued November 2008) advises that "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". The CIPFA guidance lists a number of assumptions to be considered when forming a budget, which although these directly link to the setting of a budget, the level of risk and uncertainty of these assumptions will be relevant in determining an appropriate level of reserves. These assumptions and notes to consider in relation to reserves are listed in Appendix Two.

A2.9 There has been national comment about Councils using reserves to support revenue budgets. In December 2010 the Minister for Communities & Local Government said:

"Just like any household facing challenging times, all good councils should be considering the merits of temporarily dipping into the money they have set aside as part of their plans to address immediate financial challenges, with a view to building up their reserves again in the sunnier days to come."

The Chief Finance officer is reluctant to use reserve funds, which can only be spent once, to support ongoing expenditure as that is not financially sustainable as it only delays the impact of the required budget reductions. However if the Council identifies any surplus funds from the review of reserves then this could be used to support one off expenditure. Any use of reserves for ongoing spend on an invest to save basis must be repaid and will become a call on future year's budgets.

#### A2.10 Earmarked Reserves

A2.11 Specific comments on the following reserves are listed below along with any recommendations. For the Earmarked Reserves where no specific comment has been made below, it is suggested that no changes are made, however officers can provide further detail if required. Where possible the predicted balance as at 31/3/13 on a number of reserves has been reduced by 10%.

#### A2.12 Uncommitted Earmarked Reserves – balance £3.6m 31/3/12 (£3.4m 31/3/13)

A2.13 In the 2011/12 revenue outturn report presented to Council in July 2012, it was recommended that a number of uncommitted reserves were now included within the Comprehensive Spending Review Reserve, that was originally established in 2010/11. The purpose of this reserve was identified as follows:

- short term support for the (revenue) budget while services adjust spending to new levels
- financing of any costs in relation to reducing services and therefore staff numbers
- to support any initial costs of changing service delivery that will result in future savings

Any use of this reserve for invest to save schemes must be supported by a robust business case and signed off by the Chief Finance Officer.

A2.14 The unallocated balance of £1.0m on the unringfenced performance reward grant, (in service carry forward reserve as at 31/3/12), has also now been transferred to this reserve from being held as a service carry forward. This can support the budget pressures facing the Council and its partners.

A2.15 The balance on this reserve will be impacted by the Council's current 2012/13 budget situation, where the quarter two monitoring report is reporting a significant overspend from pressures on social care – both adults and Childrens. £1.1m from this reserve has already been transferred in 2012/13 to support Childrens services. If other compensating savings can not be achieved in other budgets/services then this reserve will have to be used to fund any overspend in 2012/13.

A2.16 The cost of severance packages for staff as the Council faces budget reductions are a significant budget pressure. As a guide the cost of "exit packages" as reported in the Council's accounts, (which include schools), for 2010/11 and 2011/12 was £3m over the two years. To date in 2012/13 a further £0.6m has already been incurred. The significant budget reductions facing the Council for 2013/14 is likely to entail additional severance costs, which have been estimated at £1m, with a further £0.5m for each of the following years.

A2.17 Given the significant budget challenges facing the Council and the associated costs of reducing staff numbers it is recommended that the surplus identified on a number of reserves of approx £1.4m is transferred to this reserve and this reserve is solely used for funding any in year over spends and the costs associated with budget reductions. In addition given the uncertainty of the Council's funding levels in 2013/14, due to both the expected late announcements of grants and the late finalisation of the new Council funding legislation, any funding shortfall in setting the 2013/14 budget could have to be funded from this reserve pending identification of further budget reductions.

A2.18 Timing of Expenditure Reserves – balance £15.4m 31/3/12 (£8.9m 31/3/13)

A2.19 These reserves arise as a result of differences in timing between the reserve being established and the expenditure being incurred. Some of these are short term, such as services' carry forwards and the collection fund, where the expenditure should be incurred within 12 months. Other reserves are spreading costs over a number of years, such as the PFI sinking fund that equalises the costs of the annual unitary charge over the 25 years of the contract. No significant changes are proposed to these reserves as these are required for specific purposes or future spending plans and any proposed use of these reserves will create a future budget pressure.

A2.20 Collection Fund

The Collection Fund Adjustment Account (formally Collection Fund Reserve) is slightly different from all other reserves. Legislation requires any balance (surplus or deficit) to be applied at the next Council Tax setting to the three precepting authorities (Torbay, Devon & Cornwall Police Authority and Devon and Somerset Fire Authority). (Note Brixham Town Council as a minor precepting body does not bear any share of surplus or deficit). Any balance represents the sum collected over or under the assumed Council Tax collection rate and is normally distributed in the following financial year.

In relation to the Torbay share of the Collection Fund surplus, there is a surplus in this reserve as at 31/03/12 of £3.1m of which £2.2m was planned to be used in 2012/13. Estimates of future year surpluses will be dealt with in the report to Members on the Council Tax Base during the 2013/14 Budget Setting process and reflected in the Medium Term Resource Plan.

A2.21 Prudential Borrowing Reserve

The balance on the prudential borrowing reserve is to be used to both spread the costs of timing differences arising from the Council's statutory revenue provision calculation and the actual repayments from services for unsupported borrowing, and also to support the reduction in Council borrowing costs in future years by either repayment of Council borrowing over the next four years in line with approved Treasury Management Strategy or by voluntary revenue provision transfers. As a result the Chief Finance Officer considers it would not be prudent to significantly reduce the balance of this reserve. However due to the uncertain financial climate facing the Council it is proposed the balance on this reserve be reduced by 10%.

A2.22 Partner/RingFenced Reserves – balance £7.1m 31/3/12 (£5.6m 31/3/13)

A2.23 These reserves are outside the Council's direct control in that the reserves are linked to funds held by partner organisations, schools, economic development company or the ring fenced harbour account.

A2.24 The balance held by schools under delegated funds will change based on expenditure in schools and are likely to reduce as more Council schools become academies. A notional £0.5m annual reduction in the balances held by schools has been shown in Appendix 1.

A2.25 Specific Issue Reserves - balance £10.4m 31/3/12 (£6.2m 31/3/13)

These are reserves set aside for specific expenditure purposes.

A2.26 Insurance Reserve

The balance as at March 2012 for both the insurance reserve and the insurance provision before the addition of any current year surplus was approximately £4.5 million. The Council's insurance team in consultation with the Chief Finance Officer review the earmarked amounts on an annual basis and take advice from an insurance actuary to ensure the adequacy of the reserves. The last actuarial review was a "mini" review as at March 2012. (The next full review is due March 2014). In addition the ongoing position with Municipal Mutual Insurance (MMI) Limited and any potential calls on the Council's resources that may arise are reviewed.

Of the total of £4.5 million, £2.1 million covers earmarked amounts for specific insurance risks such as Municipal Mutual Insurance (MMI) - both Torbay Council and Devon County Council liabilities, residual Devon County Council liability relating to services transferred to Torbay in 1998, a number of uninsured risks such as environment issues and industrial diseases (e.g asbestos) and monies for risk management initiatives. The balance within the reserve and provision which is earmarked for current and as yet unknown claims as at March 2012 is £2.4 million which is broadly in line with the actuarial assessment of potential liabilities combined with an allowance for the Council's "stop loss" i.e the level the Council's exposure is limited to. However, given the Council's overall financial position it is suggested that a one off reduction in the total reserve of £0.350m is possible. This does however reduce the level of the insurance reserve, which is a risk that should be considered. Given the potential long lead in time for certain insurance claims, such as those relating to children and certain types of industrial diseases, any shortfall in this reserve may not be realised for a number of years. In addition from April 2013 the Council is responsible for the Public Health function, (from the NHS), which will result in potential additional liabilities for the Council, which may or not be fully insurable. Officers are currently reviewing the insurance implications of this transfer of responsibility.

In relation to Municipal Mutual Insurance (MMI) there is increasing uncertainty over the ability of MMI to achieve a "solvent run off of claims" which will result in a liability for the Council under the scheme of arrangement. (The MMI liability arises from the financial difficulties this insurer faced in the 1990's). In March 2012 MMI lost a Supreme Court judgment in relation to responsibility for mesothelioma cases which has increased the risk of a solvent run off not being achieved. The last MMI annual accounts (June 2012) state that the board "will be unable to foresee a position....to achieve payment of agreed claims in full and hence consideration will be given to triggering the scheme of arrangement". In November 2012 the Council was informed that the scheme of arrangement has now been triggered. In light of this increased uncertainty it is suggested that the Council's current insurance reserve for this potential liability remains unchanged.

#### A2.27 Pensions Reserve

The Council's employer's contribution rate of 17% is assessed by the actuary as the rate to generate a cash figure that will cover the Council's long term pension liabilities based on the actuarial estimate of the Council's pay costs. As the number of Council staff declines and therefore the Council's pay costs – (both from the TUPE of staff to other service providers such as TOR2 and the Economic Development Company and from budget reductions) - the cash figure generated from a 17% rate the Council will make to the fund may not meet the cash figure identified by the actuary. This is offset in part by the transfer of pension liabilities for future employment to the other service providers which will reduce the Council's forecast liability; however the Council retains the liability for those staff up to date of transfer and in some cases has guaranteed to fund future pension costs such as with TOR2.

The next actuarial review, undertaken in April 2013 – effective from April 2014, will result in higher employer contribution rates as result of the declining Council staff numbers. However as the Local Government Pension Scheme is significantly reformed from 2014, the future increase in contributions from declining numbers is likely to be offset by a reduction in future liabilities from the reforms. However to offset the shortfall in contributions up to 2014, due to declining staff numbers and therefore reduced cash contributions to the fund, the balance on the reserve will be applied as a lump sum payment to the Scheme in 2012/13. If a lump sum payment is not made any shortfall from the Council's lower cash contributions will be reflected in the Council's future contribution rate which will be a budget pressure fro 2014/15 onwards.

#### A2.28 Other Specific Reserves:

The Employment Fund (£0.3m) was set up as part of the outturn 2011/12 to support employment initiatives. The use of this reserve to support employment is being considered but has not yet been allocated to a specific proposal. However a proposal on the use of this reserve to support local businesses is expected to be presented to Council in the next few months. It is proposed this balance be reduced by 10%.

Riviera Centre Reserve (£0.250m) was set up to support the future options for the centre. This has not yet been allocated to a specific proposal. It is proposed this balance be reduced by 50%.

The TDA Capital Scheme reserve (£0.4m) is held to support regeneration schemes in the Bay. It is intended that this could be used to support the development of an innovation centre at White Rock or support any potential funding shortfall on the Brixham Regeneration project. It is proposed this balance be reduced by 50%.

Land Charges (£0.2m). Changes in central government guidance and interpretation of legislation regarding the “environmental” data Councils hold has led to considerable uncertainty regarding the charging of fees and in particular whether Councils will be required to repay fees previously charged. This issue is still being considered on a national basis which the Council will continue to monitor; therefore it is recommended that the balance on this reserve is maintained. It is proposed this balance be reduced by 10%.

On the review of reserves a number of other balances have been identified as surplus. These total £0.4m including funds from LABGI, employment issues, service carry forwards, elections and the equipment fund. It is recommended that the surplus on these reserves of approximately £0.4m identified is transferred to the Comprehensive Spending Review Reserve. In addition, where possible the level of a number of these other reserves has also been reduced by 10%.

#### A2.29 Potential Liabilities

The Council, as identified in its Statement of Accounts, has given a number of guarantees. The Council has also entered a number of contracts which could lead to a future liability such as dilapidation costs on leased in buildings. In particular the Council has provided a guarantee to bankers to the Torbay Coast and Countryside Trust for £975,000 to provide cover for the Trust’s loan and overdraft facility. If the bankers call the guarantee the Council will have to fund the £975,000 from its own resources which will probably result in the use of reserves.

In addition the Council has provided a number of guarantees for pension liabilities to services now outsourced, such as Provider Trust and the Economic Development Company, however it is unlikely that these guarantees will result in a cash payment from the Council.

### A3 Review of Provisions and other Potential Liabilities

A3.1 In addition to earmarked and general reserves the Council also holds provisions for a number of issues where the Council has a clear liability which is probable to result in a payment but the amount and timing of the potential payment is uncertain.

A3.2 As at 31/03/2012 Torbay Council’s provisions were as follows:-

<b>10/11</b>		<b>11/12</b>	<b>Change</b>
£m		£m	£m
0.6	Insurance Provision	0.6	0
0.1	Pay Modernisation (incl. schools)	0.1	0
1.3	Restructure/Budget Reductions	0.6	(0.7)
1.0	Other Provisions	0.3	(0.7)
<b>3.0</b>	<b>Total Provisions</b>	<b>1.6</b>	<b>(1.4)</b>

A3.3 The provisions above were based on the latest information as to the value of the potential liability, as such no changes in the value of these are proposed. It is expected that the majority of these provisions will be used within 2012/13 except insurance where the “time lag” on claims being notified and settled is often over one year.

## **A4 General Fund Reserve - Risk Assessment and Sensitivity/Scenario Appraisal**

- A4.1 The Council's General Fund Reserves of £4.0 million represents 3.2% of the Council's net 2012/13 budget. Using the Audit Commission profiling information this level of "unallocated financial reserves" is low compared to other unitary Councils.
- A4.2 The CIPFA guidance on reserves does not recommend a statutory minimum level of reserves. It states that "Local Authorities should make their own judgements on such matters taking into account all the relevant local circumstances which will vary between Authorities". CIPFA also state that "a well managed authority with a prudent approach to budgeting should be able to operate with a relatively low level of reserves".
- A4.3 A risk assessment of all 2012/13 budgets suggest that the maximum overspend in any year, if all services were subject to adverse pressures and where there isn't any specific service related earmarked reserve, would be £7.5 million or 6% of net revenue budget. An estimate should be added to reflect any, as yet unknown, in year budget pressures, potential Bellwin scheme claims (emergency planning) and to reflect the financial risks inherent in any significant new partnerships, outsourcing or capital developments, say £1.0 million. This would result in a required General Fund reserve of £8.5 million or 7% of net budget. The current level of General Fund Reserve will cover just under 50% of this sum.
- A4.4 This risk assessment overall is higher than the previous year as the higher value areas of volatility that were identified as a high risk last year have continued to cause pressures on the Council's revenue budget still exist, in particular the budget monitoring issues in relation to Childrens and Adult Social Care. In addition the challenges of achieving the significant budget reductions creating a higher risk of budget variations.
- A4.5 A key consideration within this risk assessment is the level of the risk of budget variances passed to partners or other suppliers via service delivery contracts. A key partner for the Council is the Torbay Care Trust as the level of funding to the Care Trust is over £42 million per annum. For 2012/13 the Care Trust and Council have not agreed to share the risk of any over or under spends on the most volatile budget area. Although the Council and Care Trust are currently discussing risk share arrangements for 2013/14 as part of the 2013/14 budget process, at this stage it is unlikely that a risk share will be agreed for 2013/14. The risk assessment above continues to reflect this significant uncertainty.
- A4.6 However a prudent risk based approach to budget setting and reserve levels will have mitigated some risks of an overspend, although it should be noted that two areas of high risk, (Childrens and Adult Social Care), have already declared significant overspends in 2012/13. It is unlikely that all budgets will be adversely affected in the same year or that there will be no underspend arising from savings or additional income. Therefore the General Fund Reserve should as a minimum be equal to 50% of the total assessed risk in any financial year which equals to 3.4% of net budget. This for 2013/14 will result in a required general fund reserve balance of £4.2 million. At this stage the current general fund balance of £4.0 million is below the target level of 3.4% of the Council's net budget requirement.
- A4.7 Following consideration of the above, in the opinion of the Chief Finance Officer, the current level of general fund reserve should not be reduced and ideally increased to reflect the higher level of risk, as balances would fall below a prudent minimum level. Therefore it is recommended that members give consideration to increase the level of this reserve as part of its Medium Term Resource Plan.
- A4.8 The 2013/14 budget to be presented to Members will also include an assurance statement from the Chief Finance Officer about the adequacy of the proposed financial reserves, in accordance with the requirements of section 25 of the Local Government Act 2003.

## Capital Investment Plan

- A4.9 It is assumed that in the circumstances of a significant overspend within the Council's capital programme this will be covered by alterations to the timing of the Council's capital programme, use of the capital contingency or from additional borrowing within the Council's approved Prudential Indicators. Any additional borrowing costs would have to be met from the Council's revenue budget.
- A4.10 The Council's capital plan has a contingency of £1.1 million – this is approximately 1% of the current four year capital plan. It should be noted that all capital projects should have contingencies within the individual project costs.

## **A5 Chief Finance Officer Statement.**

- A5.1 I am satisfied that the Council's General Fund and Earmarked Reserves, including Insurance Reserves, are adequate for the Council's Financial Plans and to meet any known or predicted liabilities over the period in which the liabilities are expected to become due for payment.
- A5.2 An updated statement on the level of reserves and their adequacy in relation the Council's financial plans, will be presented to members when Council considers the final budget proposals in February 2013.

## **A6 Governance of Reserves.**

- A6.1 Appendix 1 shows the projected balances of the reserves at the end of the current financial year and future years. These balances are based upon planned levels of spending. In the event of any unplanned expenditure occurring in the financial year current Standing Orders and Financial Regulations will apply.
- A6.2 The Reserves will continue to be reported as part of the Council's Statement of Accounts and subject to a formal annual review and challenge as part of the budget process by both members and senior officers. Councillors should consider the Councils General Fund Reserve as part of the annual budget setting process.
- A6.3 As the purpose of each earmarked reserve is clearly stated it is not considered necessary to report movements on earmarked reserves on a quarterly basis to Council or to the Overview & Scrutiny Board. Any quarterly reporting of issues relevant to earmarked reserves will be on an exception basis. Where appropriate a "withdrawal from reserve" form is completed and signed by the Chief Finance Officer and the Mayor.
- A6.4 Any budget variations that are reported to Council which can not be funded from existing revenue resources will then, as a consequence, impact on the projected balance on the General Fund Reserve.
- A6.5 Schools reserves are part of the delegated schools funding and these reserves remain at the discretion of the Head Teachers and Governing Bodies.

## **A7 Opportunity Costs**

- A7.1 Where a reserve is above the target levels, Members need to consider the opportunity costs of maintaining these reserve levels. Members need to consider that a reserve above a target level will provide benefits from reduced financial risk in that reserve and the cash flow benefits holding these levels brings from increased investment returns. These benefits need to be compared to any benefits (or opportunities) that may arise from using the reserve to support service delivery or a specific project. This "opportunity cost" of maintaining reserve levels compared to alternative spending options needs to be carefully considered.



## **A8 Risk assessment of preferred option**

### **A8.1 Outline of significant key risks**

A8.2 It is important that the issues raised in this report are considered by Members and appropriate action is taken, where necessary, to ensure that the Council has adequate reserves in the short and medium term. Failure to consider the issues raised within this report and take appropriate action could result in the Council having insufficient reserves that could adversely impact on the revenue budget.

A8.3 The two major risk facing the Council at present are the challenging budget reductions as part of the Government's Comprehensive Spending Review. There is press speculation that the deficit reduction plans could be extended beyond the current four year spending review.

A8.3 The second is the challenge of ensuring both a balanced budget for 2012/13 and a robust 2013/14 budget for social care – both adults and childrens. Both services significantly overspent in 2011/12 and are predicted to do so again for 2012/13.

## **Appendices**

Appendix 1 Council Reserves as at 31/3/12

Appendix 2 Background to Reserves and Council Policy

## 2013/14 - Review of Reserves

<b>Reserves</b>	Balance as at 1/4/12 £'000	Balance as at 1/4/13 £'000	Balance as at 1/4/14 £'000	Balance as at 1/4/15 £'000	Balance as at 1/4/16 £'000
<b>General Reserves</b>					
General Fund	3,964	3,964	3,964	3,964	3,964
	3,964	3,964	3,964	3,964	3,964
<b>Earmarked Reserves:</b>					
<b>Uncommitted Reserves:</b>					
Comprehensive Spending Issues	3,026	3,386	2,736	2,236	1,736
Change Management & Financial Strategy	150	0	0	0	0
Budget Pressures	444	0	0	0	0
	3,619	3,386	2,736	2,236	1,736
<b>Timing of Expenditure:</b>					
Capital Funding Reserve	1,119	1,722	661	261	261
Collection Fund Reserve	3,072	2,162	871	795	813
Council Elections	38	59	101	143	-20
Prudential Borrowing	2,257	1,131	1,081	1,031	981
PFI Sinking Fund	3,328	3,369	3,360	3,273	3,179
Service C/fds & Unspent Grants	5,279	297	128	11	2
Civic Hub Reserve	315	190	65	0	0
LABGI	10	0	0	0	0
	15,418	8,929	6,266	5,513	5,215
<b>Partner/Ring Fenced Reserves</b>					
Devon Audit Partnership	42	34	34	34	34
EDC Reserves (Funds paid in advance)	1,574	1,000	500	0	0
School Balances	3,518	3,018	2,518	2,018	1,518
Harbours Reserves	1,165	791	529	401	347
Public Health	436	436	0	0	0
Education Schools					
Redundancy/Retirement	331	271	211	151	91
	7,065	5,550	3,793	2,605	1,991
<b>Specific issues</b>					
Art Objects Purchased Fund	22	11	11	11	11
Crematorium	50	45	45	45	45
Asset Issues & Disposal Costs	188	137	112	87	62
Dilapidations	212	217	217	217	217
Employment Fund	305	275	225	175	125
Equipment Reserves	265	108	58	48	-12
Employment Issues	214	135	85	35	-15
Education Early Retirement	144	127	124	101	78
Insurance Reserves	3,861	3,491	3,471	3,451	3,431
IT Equipment Reserve	822	211	78	-22	28
Land Charges	192	173	173	173	173
Pearl Assurance House R &M	55	0	0	0	0
Planning Reserve	405	305	0	0	0
Regeneration Reserve	292	0	0	0	0
Riviera centre	211	125	125	125	125
Seaside Towns	50	0	0	0	0
Supporting People Commissioning	734	561	288	74	0
Tourism	161	0	0	0	0
Pension	944	0	0	0	0
TDA - Capital Schemes Reserve	427	214	214	214	214
South Devon Link Road	500	0	0	0	0
Waste Strategy	330	118	118	118	118
	10,384	6,254	5,344	4,852	4,600
Total Earmarked Reserves	36,486	24,120	18,139	15,206	13,542
<b>TOTAL RESERVES</b>	<b>40,450</b>	<b>28,084</b>	<b>22,102</b>	<b>19,169</b>	<b>17,506</b>

## **Background to Reserves, Torbay Council Policy and CIPFA advice**

### **Legislative Requirements.**

It is the responsibility for a Council's Chief Finance Officer to advise on the level of reserves that they should hold and to ensure there are clear protocols for their establishment and use. Under the Local Government Act 2003 (amended 2011) the Chief Financial Officer has a duty to report on the robustness and adequacy of Council reserves when the Council is considering its budget requirement.

This requirement is in addition to the requirements of the Local Government Finance Act 1992, which requires Councils to have regard to the level of reserves needed for meeting estimated future expenditure when calculating the budget requirement.

The Localism Act 2011 introduced new requirements in relation to reserves for the calculation of the Council Tax requirement. These include:

"such allowance as the authority estimates will be appropriate for contingencies in relation to amounts to be charged or credited to a revenue account for the year in accordance with proper practices,

the financial reserves which the authority estimates it will be appropriate to raise in the year for meeting its estimated future expenditure, and

such financial reserves as are sufficient to meet so much of the amount estimated by the authority to be a revenue account deficit for any earlier financial year as has not already been provided for".

There is no standard or guidance for a minimum level of reserves for each Council, it is the responsibility of each Council, with advice from the Chief Financial Officer, to make their own judgments on such matters taking into account all the relevant circumstances which will vary between Councils.

### **Purpose of Reserves**

Torbay Council, like most Councils, holds reserves for two main purposes

A contingency to cover the impact of unexpected events or emergency. This is often known as a Council's General Fund Reserve. This reserve also, in effect provides a working balance to help cushion the impact of uneven cash flows.

A means of building up funds often referred to as Earmarked Reserves, to meet known or predicted liabilities. These Earmarked Reserves could include:

- Sums set aside for known or anticipated liabilities.
- Sums set aside for major schemes.
- Insurance reserves.
- Trading reserves – e.g Harbours.
- Reserves retained for Service Department use.
- School balances.
- Council Tax Collection Fund Balances.

The annual Review of Reserves is a key part of a Council's Risk Management process. If a reserve is assessed not to be adequate, an appropriate contribution from future year's revenue budgets should be planned for, conversely if a reserve is assessed as over provided, the surplus can be used as part of future year budget funding. This review focuses on earmarked reserves and the Council's general fund reserve.

There are other reserves that Councils hold that arise out of legislation and accounting rules but

these are not “cash” backed and can not be used for any other purpose. These include revaluation reserve, capital adjustment account and the pension reserve.

## **Policy for Reserves**

It is considered good practice for Councils to have “a soundly based policy on the level and nature of reserves and balances that has been approved by members and reflected in the budget and medium-term resource plan”. The following is the Council’s current policy for reserves:

### **Earmarked Reserves:**

“Torbay Council will hold earmarked reserves to meet known or specified liabilities. The purpose of each reserve will be clearly stated when established along with a suggested target range for the balance on the reserve. Each reserve will be allocated to the responsibility of a service manager who will at least twice a year review the reserve for both relevance and adequacy. This is to ensure a thorough understanding of the needs and risks of the service/function to which the reserve relates. If a Reserve is assessed as not required or a change in use is requested this will be reported in the next Budget Monitoring Report to Council”.

### **General Fund Reserve:**

“The Council will maintain a General Fund Reserve as a contingency to cover the impact of unexpected events or emergency. The Council will at least annually review the reserve and assess the target range for the balance on this reserve in light of the Council’s overall financial position”.

### **Financial Planning**

“The Council will reflect the results of its policy on reserves in its Medium Term Resource Plan and other financial planning such as the Treasury Management Strategy and Capital Plan. The approved level of balances will be monitored to ensure the Council’s financial standing is sound and supports the Council in the achievement of its long term objectives”.

Cabinet on 23/10/07 approved (report 271/2007 refers) the Council’s policy for Reserves as set out in that report which included that the policy be endorsed not only for 2008/09 but also for all future years. Members, however, are free to recommended changes to the policy if required.

## **Monitoring of Reserves**

The Council monitors and maintains its levels of reserves and balances within the range determined by its agreed policy. Details of each reserve are contained on a specific database which estimates a target range for each reserve. As the use of Reserves tends to be planned there isn’t a requirement for detailed quarterly monitoring of reserves. Any significant changes in Reserve use or activity will be reported on an exception basis to Council during the quarterly budget monitoring process. The detailed monitoring of reserves is undertaken on an annual basis by this detailed Review of Reserves. The Council will also consider any appropriate Reserve movements as part of the Council’s outturn reporting.

### **Principles to Assess the Adequacy of Reserves and Scenario Analysis**

The CIPFA guidance on Reserves and Balances (issued November 2008) advises that “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, such as budget pressures”. The CIPFA guidance lists a number of assumptions to be considered when forming a budget, which although these directly linked to the setting of a budget, the level of risk and uncertainty of these assumptions will be relevant in determining an appropriate level of reserves.

The assumptions and notes to consider in relation to the current conditions are listed below:

<b>Budget Assumption</b>	<b>Sensitivity</b>	<b>Financial Standing and Management</b>
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Inflation & interest rates	<p>Inflation is, on balance, a low risk at the current level.</p> <p>Interest rates are a key factor. A 1% change in rates can result in a £0.7m variation</p>	<p>With the current rates of both RPI and CPI inflation is a risk on a number of Council budgets such as utilities. However with the current pay freeze and economic conditions keeping some other inflationary pressures overall inflation rates area low risk.</p> <p>Interest rates (bank base rate) are currently 0.5% and are expected to stay at that level of most if not all of 2013/14. This has an adverse impact on Council investments. The Council's medium term borrowing requirement is already secured at fixed rates.</p>
Level and Timing of Capital Receipts	A 10% drop in value has an impact of reducing receipts by £0.5 million	<p>As a result of the economic conditions there has been a drop in the level of receipts received by the Council and the value of potential receipts on some assets have been reassessed at a lower level.</p> <p>To support the generation of capital receipts there is the Asset Rationalisation Plan which aims to generate the required level of receipts over the four year life on the plan. Due to the low bank rate the major risk associated with capital receipts is the value rather than the timing although a delay in receipts will reduce investment income and could lead to temporary borrowing.</p>
Treatment of Demand led pressures	<p>An average childcare placement costs £40k per annum.</p> <p>A 1% increase in the employer's contribution rate is £0.4m</p>	<p>Certain budgets are often volatile due to changes in demand levels such as for both adult and childrens' social care (from a rising number of children on the "at risk" list) which indicate that this is an area of potential risk. In year recovery plans and planning for the management of future year demand will be critical.</p> <p>The reducing number of Council staff contributing to the pension scheme reduces the Council's cash contributions to the fund which is likely to lead to higher employer contributions in the future. (Subject to any reductions on employee benefits from changes to the scheme).</p>
Treatment of planned efficiency savings/productivity gains/new income streams		<p>The Council is faced with significant budget reductions over the next four years. Some of the savings required may not be achievable from April 2012 due to the time lag in developing and implementing significant changes or cuts to services.</p> <p>Efficiencies are identified as part of the budget setting process and are assumed to be achievable when set as part of a setting a balanced budget.</p> <p>Future efficiencies arising are not assumed until realised.</p>
Financial risks inherent in any new funding partnerships, outsourcing or major capital developments.	A 1% variation on the whole capital plan is approx. £1m	<p>This is a key risk for the Council with the level of both any service changes and its capital programme.</p> <p>Each project is managed in terms of risk and has a project board, however consideration could be given to earmarking reserves to mitigate any potential risk</p>
Availability of reserves, government grants and other funds to deal with major contingencies and the adequacy of provisions	A 1% change on the Council's net spend is £1.25 million	The Council's insurance reserve is separately reviewed on an annual basis. The Council would have access to the Bellwin scheme for uninsurable major incidents.
General financial climate		The impact of interest rates, inflation and capital receipts have already been noted, however there are other risks

		<p>associated with the current economic conditions. These would include lower income levels on services such as land charges and planning, lower levels of tax collection and higher levels of bad debts being incurred etc</p> <p>The money market conditions and in particular the issues associated with Icelandic banks has highlighted risks associated with Council loans and investments. The Council has had no experience of default of any of its investments. The arrangements to manage this risk are outlined in the annual Treasury Management Strategy.</p>
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The CIPFA guidance issued in November 2008 was, in part, a response to a higher level of scrutiny of risk arising both from the default of Icelandic banks – including a significant number of local authority investments, and from the costs of the major floods in the summers of 2007 and 2008. The conclusion is that Councils should have adequate insurance cover and an appropriate level of reserves to enable them to manage the demands placed on them from such major circumstances.

### **Links to other Strategies**

The level of reserves has clear links to a number of other Council plans and strategies. The level of reserves will depend on and be incorporated in these other documents. These include:

#### **Capital Investment Plan:**

A number of reserves are linked to the purchase or replacement of assets. This expenditure will be treated as Capital Expenditure and funded from the earmarked reserve.

#### **Medium Term Resource Plan:**

The results of this review of reserves, in particular the General Fund Reserve balance, will need to be incorporated into the Medium Term Resource Plan. In addition any significant under or over provision on earmarked reserves will need to be included.

#### **Treasury Management Strategy:**

The Treasury Management Strategy includes the implications of the level of reserves held for potential cash flow for investment decisions. In addition it will assess the cash flow and financing implications of any significant movement in reserves.