

Lancashire Combined Fire Authority

Meeting to be held on 20 February 2023

Reserves and Balances Policy (Appendix 1 refers)

Contact for further information:

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Table 1 Executive Summary and Recommendations

Executive Summary

The Fire Authority needs to hold reserves to meet potential future expenditure requirements.

The reserves policy is based on guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA).

The policy explains the difference between general reserves (those held to meet unforeseen circumstances) earmarked reserves (those held for a specific purpose) and provisions (where a liability exists but the extent and/or timing of this is uncertain). In addition, the policy identifies how the Authority determine the appropriate level of reserves and what these are.

The policy confirms that the level of and the appropriateness of reserves will be reported on as part of the annual budget setting process and as part of the year end accounting process.

The most significant issues are: -

- General reserves are sufficient to meet current requirements. However, there is a great deal of uncertainty as to the level of costs, and who will bear these, relating to changes to the Firefighter pension scheme.
- Earmarked reserves will reduce over the 5-year period.
- The PFI reserve reduces over the remaining life of the two schemes.
- Capital reserves will be fully utilised over the 5-year programme.
- Provisions will remain at broadly the same level.

Recommendation

The Authority is requested to approve the policy and note the Treasurer's advice on the level of reserves included within it.

Reserves and Balances Policy

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

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

The reserves policy complies with these requirements.

General Reserves (General Fund)

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

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

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

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

Table 2 Summary of General Reserves (General Fund)

Name	General Reserves (General Fund)
Purpose	This covers uncertainties in future years budgets, such as: <ul style="list-style-type: none"> • future grant settlements being lower than forecast; • higher levels of inflation than budgeted;

	<ul style="list-style-type: none"> • increasing cost of and changes to pensions; • service demands increasing, putting additional pressure on demand led budgets; • changes in legislation impacting on future service provision; • potential cost of industrial action.
Utilisation	This is utilised to offset any in-year overspend that would occur when comparing budget requirement to the level of funding generated.
Controls	The utilisation of this is agreed as part of the annual budget setting process. Any further utilisation requires the approval of the Resources Committee.
Review	The adequacy of this is reviewed annually, as part of the budget setting process.

Review of Level of Reserves

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

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

There remains a great deal of uncertainty over long term funding, as a result, the anticipated multi-year settlement has been postponed again. The Local Government Finance Settlement only covered 2023/24, although the policy statement that accompanied it stated "The core settlement will continue in a similar manner for 2024-25. The major grants will continue as set out for 2023-24: Revenue Support Grant will continue and be uplifted in line with Baseline Funding Levels". Whilst this provides a basis for estimating future funding increases, as set out in the revenue budget paper, it does not provide any certainty.

Furthermore, the outcome of the fair funding review of relative needs and resources and the Government intention to move to greater retention of Business Rates have also been postponed.

The position in terms of pay awards has still not been resolved, however the likelihood of this being significantly higher than the budgetary allowance and the likelihood of industrial action have both reduced as a result of the latest pay offer.

Whilst future pension costs remain uncertain, with Authorities still awaiting definitive guidance on how to implement changes following the McCloud judgement, and with the next revaluation of the firefighter pension scheme being due this year, the draft budget for 2024/25 already includes a 3% allowance for this.

As such the Treasurer considers it prudent to reduce the minimum target reserves level to £3.75m, 5.5% of the 2023/24 net revenue budget, reflecting the level of uncertainty. (Note, it may be possible to reduce this minimum level further if the current grey book 2 year pay offer is accepted.) This is slightly higher than the 5% threshold identified by the Home Office above which the Authority is required to justify why it holds the level of reserves, reflecting the increasing uncertainty about future funding, pension costs and pay awards.

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

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

Whilst the settlement provides greater flexibility to increase council tax in 2023/24, this is a one-off relaxation of the referendum principles and current indications are that it will not be repeated in future years. Hence the scope to increase council tax in future years to restore depleted reserves is limited, without holding a local referendum. Therefore, any maximum reserve limit must take account of future anticipated financial pressures and must look at the long-term impact of these on the budget and hence the reserve requirement. Based on professional judgement, the Treasurer feels that this should be maintained at £10.0m.

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

Level of General Reserves

The overall level of the general fund balance, i.e., uncommitted reserves, anticipated at the 31 March 2023 is £4.0m, providing scope to utilise approx. £0.25m of reserves.

The draft budget as presented elsewhere on the agenda identifies a funding gap of £0.3m in 2023/24, which could be met from a combination of a drawdown against this reserve and additional in-year savings. The Treasurer therefore considers this reserve is at an appropriate level.

Looking at the medium term the need to drawdown reserves will be affected by:-

- Council tax – The revenue budget assumes that council tax is increased by the maximum permissible each year, enabling the Service to deliver a balanced budget each year, after allowing for relatively low level of reserve drawdown/additional savings. If this is not the case, then we may need to utilise reserves in future years to balance the budget.
- Pension costs – the revenue budget assumes that the only pension costs that fall on the Service are employer contributions, and that all other costs are met by the Government via the Pension Holding Account. If this is not the case, then reserves would be required to meet these one-off costs which will be very significant. Furthermore, it assumes that the employer contribution rate will increase by 3% following the next tri-annual revaluation exercise, but at the present time no details are available hence contribution rates could increase by a greater amount.
- Future funding - the revenue budget assumes future funding increases by 5% in 2024/25 followed by 2% increases thereafter. If that is not the case and it is frozen as part of the next multi-year settlement, this would reduce funding levels by £0.6m each year, a cumulative reduction of £1.9m over the medium-term financial strategy, and this would impact on the need to drawdown reserves.
- Future inflation - the revenue budget assumes pay awards running at 5% in 2023/24 before returning to the Government's 2% target. If this is not the case each 1% more than this increases the recurring budget requirement by £0.4m, i.e., £2.9m over the next 5 years, which may impact on the usage of reserves.

At the present time, the Medium-Term Financial Strategy (MTFS) identified funding gaps in the next 4 years. Assuming 50% of these are met by additional in-year savings with the balances being drawdown from this reserve, we will potentially see this reserve falling to £3.2m by March 2027. This is below our current minimum requirement. However, the forecasts are subject to a number of variable factors, as set out above, and these will continue to be reviewed to refine forecasts and ensure that reserves remain above our minimum threshold throughout the duration of the MTFS.

Earmarked Reserves

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

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

Table 3 Summary of Earmarked Reserve

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

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

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

Level of Earmarked Reserves

The following table provides a breakdown of the £2.6m of earmarked reserves forecast to be held at 31st March 2023, and a forecast of the anticipated position as at 31 March 2028: -

Table 4 Earmarked Reserve Balances

	Forecast at 31 March 2023	Forecast at 31 March 2028	
	£m	£m	
Specific Grant Carried Forward	0.2	-	This reserve carries forward unspent specific grants <ul style="list-style-type: none"> • Protection Uplift Grant • Building Risk Review Grant • Grenfell Infrastructure Grant • ESMCP Grant • Efficiency Grant We anticipated utilising these in the new financial year. There are no contractual or legal obligations against this reserve.
DFM Reserve	0.3	0.3	Devolved Financial Management Reserve enables budget holders to carry forward any surplus or deficit from one financial year to the next, within prescribed limits.

			<p>This reserve provides greater flexibility to individual budget holder to carry forward underspends within their own budget area to meet future costs and optimise the use of resources. Examples of areas where these balances have been used previously would be one-off replacements of equipment, or enhancement to station facilities etc.</p> <p>The levels of individual DFM reserves are reviewed each year as part of the revenue outturn/annual accounts process, to ensure that they are reasonable and that budget holders are not building up excessive reserves. As a result of this exercise, the Authority has stripped out £0.1m and transferred this into the capital funding reserve (referred to later in the report).</p> <p>At present there are no contractual or legal obligations against this reserve, as any such commitments would be included in the base revenue budget.</p>
Insurance Aggregate Stop Loss (ASL)	1.1	1.1	<p>The Authority has Aggregate Stop Losses (ASLs) on both its combined liability insurance policy (£0.4m) and its motor policy (£0.3m). This means that in any one year the Authority's maximum liability for insurance claims is capped at the ASL. As such the Authority can either meet these costs direct from its revenue budget or can set up an earmarked reserve to meet these. Within Lancashire we have chosen to meet the potential costs through a combination of the two. Hence the amount included in the revenue budget reflects charges in a typical year, with the reserve being set up to cover any excess over and above this. As such the reserve, combined with amounts within the revenue budget, provides sufficient cover to meet 2 years' worth of the maximum possible claims, i.e., the ASL. (It is worth noting that the revenue budget allocation has also been reduced in recent years reflecting the claims history. Without holding this reserve to cushion any major claims that may arise this would not have been possible.)</p> <p>None of this reserve is legally committed at the present time, although as soon as a claim arose this position would change.</p>

Prince's Trust	0.4	0.4	<p>This reserve has been established to balance short term funding timing differences and to mitigate the risk of loss of funding and enable short term continuation of team activities, whilst alternative funding is found.</p> <p>Without this reserve any significant loss of funding would have an immediate impact on our ability to deliver the PT programme, and hence improve the lives of younger people. This reserve has been capped at £0.5m.</p> <p>There are no legal or contractual commitments against this, however forecasts show this budget reducing reflecting the uncertainty over future funding.</p>
Apprentices	0.1	-	<p>This reserve was created from previous in-year underspends relating to the appointment of apprentices, which was delayed awaiting national developments.</p> <p>As such the reserve was set up to offset some of the pay/training costs that will be incurred in future years, with the balance being met direct from the revenue budget. This clearly contributes to addressing apprenticeship targets, set by the Government, as well as addressing capacity issues within departments.</p> <p>There are no contractual commitments against this.</p>
Innovation Fund	0.5	0.1	<p>The Authority created an Innovations Fund to meet costs arising from new initiatives/developments which improve service delivery or fire fighter safety, but which are not included in the capital programme. Any requests to utilise the fund require the approval of the Executive Board. The capital program shows £0.4m of this being utilised in 24/25 to fund the provision of a second Vehicle Mounted Data Systems (VMDS) unit in each fire appliances, thus enhancing the capabilities of crews whilst mobile.</p> <p>If the opportunity arises this will be topped up from future savings.</p> <p>None of this reserve is contractually or legally committed at the present time.</p>
	2.6	1.9	

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

PFI Reserve

This reserve was created specifically to smooth out the annual net cost to the Authority of the existing PFI schemes and will be required to meet future contract payments.

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

Table 5 Summary of Earmarked Reserve

Name	Earmarked
Purpose	This covers monies set aside to smooth out costs associated with the Authorities PFI schemes and is required to meet future contract payments.
Utilisation	This reserve can only be used for the specific purpose for which it was established, i.e., meet future PFI costs.
Controls	The utilisation of this is set out in the budget agreed at the start of the year, any variance in requirements from this are agreed by the Treasurer as part of the budget setting/revenue outturn/annual accounts processes.
Review	The level of the reserve is reviewed each year as part of the revenue outturn/annual accounts process to ensure these are reasonable and remain relevant.

Level of PFI Reserve

At 31 March 2023, the Authority anticipates holding £4.9m of PFI reserve. The reduction of this reserve in subsequent years reflecting its drawdown to offset future charges, with the reserve reducing to £3.7m by March 2028.

Assuming the Retail Price Index returns to 3% in future years the whole of this reserve is contractually committed over the next 20 years.

Based on this the Treasurer believes this is adequate to meet future requirements.

Capital Reserves and Receipts

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

Capital Receipts are generated from the sale of surplus assets, which have not yet been utilised to fund the capital programme. Under revised regulations receipts generated between April 2016 and March 2020 can be used to meet qualifying revenue costs, i.e., set up and implementation costs of projects/schemes which are forecast to generate on-going savings. The on-going costs of such projects/schemes do not qualify. Whilst the Authority currently holds £1.7m of capital receipts only

£0.2m of this arose in the relevant period. Given the small amount eligible we do not currently have any plans to use this in line with new regulations and hence for the purpose of planning all capital receipts will be used to meet future capital costs, not qualifying revenue expenditure.

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

Table 6 Summary of Capital Reserves and Receipts

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

At 31 March 2023, the Authority anticipates holding £20.3m of capital reserves and receipts. Based on the capital programme presented elsewhere on this agenda, the Authority anticipate fully utilising these by 31 March 2027. Of the total reserve £5.0m is contractually committed.

Based on this, the Treasurer believes these are adequate to meet future requirements in the short to medium term but recognises that they will be exhausted March 2025.

Summary Reserve Position

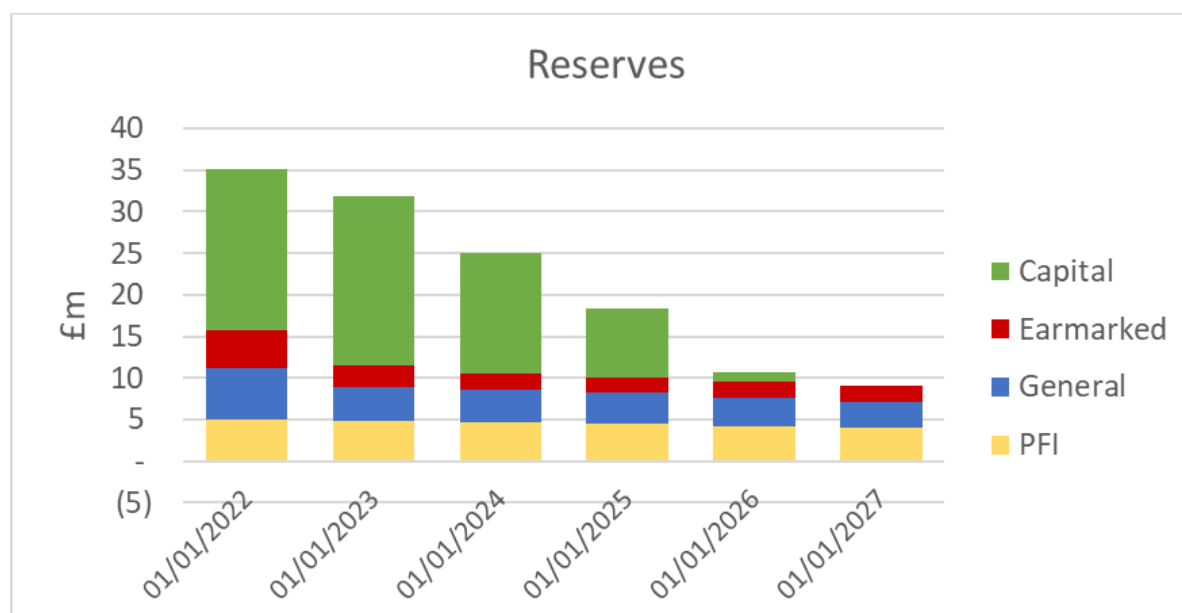
The following table sets out the anticipated position in terms of reserves and balances, a more detailed year on year analysis by reserve is attached as appendix 1: -

Table 7 Summary Use of Reserves March 22 to March 28

	General Reserve	Earmarked Reserve	PFI Reserve	Capital Reserves & Receipts	Total Reserves & Balances
	£m	£m	£m	£m	£m
Balance 31/3/22	(6.0)	(4.7)	(5.1)	(19.4)	(35.1)
Change in year	2.0	2.1	0.2	(0.9)	3.3
Balance 31/3/23	(4.0)	(2.6)	(4.9)	(20.3)	(31.8)
Change in year	0.2	0.1	0.2	5.8	6.2

Balance 31/3/24	(3.9)	(2.0)	(4.7)	(14.5)	(25.1)
Change in year	0.2	0.0	0.2	6.3	6.7
Balance 31/3/25	(3.7)	(1.9)	(4.5)	(8.2)	(18.3)
Change in year	0.4	0.0	0.2	7.0	7.6
Balance 31/3/26	(3.3)	(1.9)	(4.3)	(1.2)	(10.7)
Change in year	0.2	0.0	0.2	1.2	1.6
Balance 31/3/27	(3.1)	(1.9)	(4.0)	0.0	(9.1)
Change in year	(0.0)	0.0	0.3	0.0	0.2
Balance 31/3/28	(3.2)	(1.9)	(3.7)	0.0	(8.8)

Graph 1 Reserve Balances March 22 to March 28



The level of reserves reduces by over £20m over the next 3 financial years, reflecting the scale of the capital programme. Our general reserve remains above our minimum requirement throughout the period, reflecting the increase in council tax included in the revenue budget report. The position will be subject to significant change as pension costs, funding, inflation, pay awards etc become clearer in future years. The annual refresh of this policy will identify the impact of any changes as they develop.

Provisions

In addition to the above reserves the Authority also has two provisions to meet future estimated liabilities: -

Insurance Provision

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

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

Table 8 Summary of Insurance Provision

Name	Insurance Provision
Purpose	This covers monies set aside to meet future insurance claims.
Utilisation	Once set up the provision can only be utilised to meet insurance claims.
Controls	The utilisation of these is reported on an annual basis as part of the year end outturn report presented to Resources Committee.
Review	The level of the provision is reviewed annually based on existing and anticipated outstanding insurance claims to ensure these are reasonable and remain relevant.

This provision stood at £0.6m at 31 March 2022. Given the uncertainty in terms of future insurance claims we have assumed that the provision will be maintained at this level throughout the 5-year period. There are no existing legal obligations associated with this provision, as the legal obligation only arises when settlement of outstanding claims is agreed.

Business Rates Collection Fund Appeals Provision

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

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

Table 9 Summary of Business Rates Collection Fund Appeals Provision

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

At 31 March 2022 this provision stood at £0.9m to cover anticipated costs of outstanding business rates appeals. Whilst a significant element of this will be utilised in the current financial year, reflecting the settlement of outstanding appeals, it is impossible to accurately predict the extent of this usage or the need for any additional provision to meet appeals that arise in year, until such time as a full review is undertaken by billing authorities as part of the financial year end process. Therefore, for the purpose of this report we have assumed that the level of business rates appeals provision remains unchanged. Until the outcome of any appeal is known there is no legal obligation arising from the appeal.

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

Financial Risk

There is a risk that the level of reserves will not be sufficient to meet future requirements, this policy and the subsequent reporting mechanism is designed to mitigate this.

HR Risk

None.

Equality and Diversity Implications

None.

Environmental Impact

None.

Business Risk Implications

The management of reserves forms a key element of our budget strategy. Having an agreed policy, within which we can manage our reserves, provides clearer

accountability, and reduces the risk of the Authority maintaining an inappropriate level of reserves, either too high or too low.

Local Government (Access to Information) Act 1985
List of Background Papers

Paper: Revenue and Capital Budget Reports

Date: 2023

Contact: Keith Mattinson

Reason for inclusion in Part 2 if appropriate: N/A

Appendix 1

Reserve Balances by Year

Table 11 Detailed Use of Reserves March 23 to March 28

	31/03/23	31/03/24	31/03/25	31/03/26	31/03/27	31/03/28
	£m	£m	£m	£m	£m	£m
General	4.0	3.9	3.7	3.3	3.2	3.2
Earmarked						
Specific Grants	0.2	-	-	-	-	-
DFM	0.3	0.3	0.3	0.3	0.3	0.3
Insurance ASL	1.1	1.1	1.1	1.1	1.1	1.1
Princes Trust	0.4	0.4	0.4	0.4	0.4	0.4
Apprentices	0.1	-	-	-	-	-
Innovation Fund	0.5	0.2	0.1	0.1	0.1	0.1
	2.6	2.0	1.9	1.9	1.9	1.9
PFI	4.9	4.7	4.5	4.3	4.0	3.7
Capital Reserves & Receipts	20.3	14.5	8.2	1.2	-	-
Total Reserves	31.8	25.1	18.3	10.7	9.1	8.8
Provisions						
Insurance	0.6	0.6	0.6	0.6	0.6	0.6
Business Rate Collection Fund Appeals	0.9	0.9	0.9	0.9	0.9	0.9
	1.5	1.5	1.5	1.5	1.5	1.5
	33.83	26.6	19.8	12.2	10.6	10.3