




DECISION PAPER

DECISION: 2019/05	DATE: 23 APRIL 2019
TITLE: RESERVES STRATEGY 2019/20	
REPORT BY: STEVE FREEMAN, CHIEF FINANCE OFFICER	
APPENDIX A REFERS	
Executive Summary	
<p>This report sets out the Commissioner's Reserves Strategy for 2019/20.</p> <p>This strategy forms an integral part of the Commissioner's Medium Term Financial Planning process that enables the effective planning and control of the revenue budget and the capital investment programme.</p>	
Recommendation	
<p>The Police and Crime Commissioner is asked to:</p> <ul style="list-style-type: none">• Approve the Reserves Strategy for 2019/20• Agree to maintain a general reserve at a level that is between 3% and 5% of the annual revenue budget.• Approve the use of earmarked reserves to support organisational change and provide investment in the capital investment programme as set out in Appendix 'A'.• Review the reserves strategy on an annual basis.• Agree to make contributions into specific reserves if the opportunity arises.	
Signature	
Police and Crime Commissioner	
Date	23rd April 2019

PART II

1. Background and Advice

The report attached at Appendix A sets out the Police and Crime Commissioner's Reserves Strategy for 2019/20.

2. Links to the Police and Crime Plan

The Reserves Strategy forms an integral part of the overarching financial strategy for the organisation which is vital to the delivery of operational policing and therefore supports the delivery of frontline policing as determined by the Police and Crime Plan and the Chief Constable's Strategic Strategy.

3. Consultations

4. Implications:

a. Legal

There are no legal implications directly arising from this report

b. Financial

The Reserves Strategy ensures the appropriate management of the Commissioner's resources and delivers investment in the Commissioner's agreed capital investment programme.

c. Equality Impact Assessment

There are no direct equality implications in the making of this decision.

d. Data Protection Impact Assessment

There are no direct Data protection implications in the making of this decision.

5 Risk Management

The Reserves Strategy ensures that any risk associated with the management of the Commissioner's resources is managed in an appropriate and effective manner.

6. Background Papers

None

7. Public access to information

Chief Executive Officer (Monitoring Officer)

I have been informed about the proposal and confirm that financial, legal and equalities advice has been taken into account in the preparation of this report. I am satisfied that this is an appropriate request to be submitted to the Police and Crime Commissioner for Lancashire.

Signature  Date 23/4/2019

Police and Crime Commissioner for Lancashire

Reserves Strategy – 2019/20

1. Introduction

- 1.1. This paper reports the estimated level of reserves currently held by the Commissioner and proposes a Reserves Strategy for approval by the Commissioner
- 1.2. The reserves strategy sets out the use of general reserves and earmarked reserves (which are set aside for a specific purpose) and forms part of the Medium Term Financial Strategy which is updated regularly and reviewed by the Commissioner and Chief Constable.
- 1.3. In preparing this report the legislative and other requirements for the holding of reserves has been reviewed. The current financial position in respect of both the revenue budget and the capital programme, assessments of current and future risk, reserve levels in other Forces and views expressed by government, peers and the public have also been considered.

2. Legislation and guidance regarding the holding of a general reserve

- 2.1. Legislation and CIPFA guidance (2014) require that a general reserve is maintained but do not stipulate the level of that general reserve. However, the guidance does require the PCC to consider strategic, operational and financial risk when determining reserve levels with advice from the Treasurer. In addition the Local Government Act 2003 requires the S151 officer (the PCC's Treasurer) to report on the level of reserves annually, the planned usage and the opportunity cost of holding those reserves.
- 2.2. CIPFA's Guidance Note on Local Authority Reserves and Balances(1) states that a general reserve is required to act as "a working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – this forms part of general reserves". A general reserve is also required to act as "a contingency to cushion the impact of unexpected events or emergencies – this also forms part of general reserves."
- 2.3. Maintaining a general reserve ensures compliance with the Local Government Finance Act 1992 (2) which states that authorities must "have regard to the level of reserves needed for meeting estimated future expenditure when calculating the budget requirement."
- 2.4. As part of the annual audit of the Commissioner's Statement of Accounts the external auditors provide an opinion on the level of reserves held by the Commissioner thereby providing an external scrutiny of the level of reserves being held.

3. Factors to consider in deciding on reserve levels

3.1. Overall financial position and adequacy of financial control

- 3.1.1. In setting the level of the general reserve it is important to bear in mind Lancashire's overall financial position and the adequacy of financial control in operation.
- 3.1.2. The overall financial position has been considered by the PCC as part of the budget process and medium term financial planning, which has taken account of the impact of the government's austerity measures.
- 3.1.3. It is also important to remember the context of the Medium Term Financial Strategy (MTFS) agreed as part of the budget process so that the PCC continues to comply with CIPFA's Guidance Note on Local Authority Reserves and Balances which suggests that "Advice should be given on the adequacy of reserves over the lifetime of the medium term financial plan".
- 3.1.4. The use of general reserves does afford the PCC some flexibility in managing the MTFS and the Capital Programme over a number of years where future investment is considered against the pressure placed upon the annual revenue budget.

3.2. Risk exposure and risk assessment

- 3.2.1. Reserve levels must be considered in the context of risk if we are to comply with CIPFA's guidelines which state that "in order to assess the adequacy of unallocated general reserves.....Chief Financial Officers should take account of the strategic, operational and financial risks facing the organisation."
- 3.2.2. Whilst risk exposure and mitigation of that risk may not necessarily drive a material increase in spending, it will influence the level of general reserves year by year.
- 3.2.3. The key risks currently relevant to the level of general reserves now and in the future are;
 - Future Funding Gap – the risk that due to the increase in Demand faced by the force and the real reduction in funding from government, the increased resource requirements will have a significant effect on already stretched financial resources. This pressure is likely to impact on operational policing which in turn has an impact on the achievement of targets in the PCCs Policing Plan.
 - Uncertain central funding after 2019/20 due to proposed changes to the Comprehensive Spending Review (CSR) taking place in 2019.
 - The ongoing use of "top slicing" that has increased every year since its introduction which in turn increases uncertainty over the level of funding individual forces will have in future years.

3.3. Public opinion

3.3.1. A key factor in determining a General Reserves Strategy continues to be public opinion. The public's acceptance of the precept is partly reliant on the understanding that the precept is spent on policing and that only a reasonable and prudent amount of any over-funding is being stored away as a General Reserve. Conversely, when unforeseen expenditure arises, such as with the anti-Fracking protest in Lancashire, it is likely that the public would expect the organisation to have sufficient resources to cover the expense without recourse to overspend.

4. General reserve levels and their use

4.1. Use of General Reserves

4.1.1. The current strategy for general reserves levels is hold an amount that represents between 3% and 5% of the annual revenue budget. This reflects the consideration of the factors set out above and has been confirmed as appropriate by the external auditors in their review of the Statement of Accounts for 2018/19.

4.1.2. The Commissioner's general reserves are available to support the medium term financial planning process and to provide a source of funding for investment in the capital programme if required.

4.1.3. The use of general reserves does not provide an on-going revenue funding stream to support the revenue account position. However, notwithstanding issues related to risk and medium term planning, it is reasonable to use reserves to fund initiatives in the short term that themselves had on-going positive revenue funding implications. These initiatives are known as "invest to save" options.

4.2. In order to assess the adequacy of unallocated general reserves (otherwise known as general balances) when setting the budget the PCC, on the advice of the two chief finance officers, should take account of the strategic, operational and financial risks facing the authority. This assessment of risk should include external risks, such as flooding, as well as internal risks, for example the ability to deliver planned efficiency savings.

4.3. Table 1 examines how Lancashire currently complies with the 7 key CIPFA principles to assess the adequacy of reserves.

Table 1: Compliance with the 7 key principles

Budget assumptions	Current situation in Lancashire
The treatment of inflation and interest rates	<p>The PCC and Chief Constable (CC) make full and appropriate provision for pay and price rises.</p> <p>An informed assessment is made of interest rate movements.</p> <p>All individual expenditure and income heads in the revenue budget are prepared and published at estimated outturn prices.</p>

Estimates of the level and timing of capital receipts	The PCC and CC make a prudent assumption of future capital receipts.
The treatment of demand led pressures	<p>The Force is required to operate and manage within its annual budget allocation.</p> <p>The PCC retains a central reserve to help finance large scale or corporate operations or issues, the 'Operational Policing Reserve'</p> <p>In addition the CC holds a delegated 'DFM reserve' to deal with day to day changes in demand and pressure.</p> <p>In 2018/19 the pressure placed on the budget in respect of the policing of anti-fracking protests in Lancashire meant that for the first time in more than 10 years a draw down on the operational policing reserve was needed, even with the award of special grant by the Home Office. A number of significant operations were live in 2019/20, the cumulative effect of these may require further draw down from this reserve.</p> <p>The Force has already identified £3.3m of cash savings which will be removed from the budget over the next four years (2019/20 to 2022/23). This means that £87.9m of cash savings have been removed from the base budget since 2011/12. A funding gap of £21.7m has been identified to 2022/23 which means that over £106m of savings will have been delivered by 2022/23.</p> <p>This cumulative level of budget reduction will inevitably mean that operational budgets will come under even greater pressure and/or risk of overspending in future years.</p> <p>Some government grants are announced annually in advance and are cash limited. Any new policing pressures arising during the year will have to be funded from the PCC and Constabulary's own resources.</p> <p>The PCC and CC have created a number of earmarked revenue reserves to help finance specific, ad-hoc, expenditure commitments. Appropriations are made to and from these reserves on an annual basis, as required.</p> <p>Finally, general balances are used as a last resort to manage and fund demand-led spending pressures.</p>
The treatment of planned efficiency	The Force has consistently achieved its annual savings target over the last 10 years.

savings/productivity gains	As explained above, over £87m of cash savings has already been taken out of the base budget with a further £21.7m required over the next four years.
The financial risks inherent in any significant new funding partnerships, collaboration, major outsourcing arrangements or major capital developments	<p>The financial consequences of partnership collaboration working, outsourcing arrangements or capital investment are reported to the PCC as part of the medium term planning process. Where relevant, any additional costs are incorporated in the annual revenue budget and/or capital programme.</p> <p>There is clearly a risk that local authority partners will continue to withdraw funding as their own budgets are squeezed, or that the continued financial viability of private sector commercial partners will be exposed to risk in the face of an economic recession.</p>
The availability of reserves, government grants and other funds to deal with major contingencies and the adequacy of provisions	The PCC has created a number of earmarked revenue reserves and provisions to meet specific expenditure items. These are referred to in more detail in paragraph 5 below.
The general financial climate to which the authority is subject.	<p>In September 2018 Police officers pay was increased by 2% and in the latest negotiations larger increases are being requested in future years, increasing the potential pressure on Police Funding.</p> <p>A Spending Review will be undertaken in 2019 that will determine future years' funding for the sector against a background of demands for savings from government departments by the Treasury. This delivers uncertainty which adds to the potential future risk for funding for Lancashire.</p> <p>Increasingly the burden of funding forces is being passed to local council tax payers by central government and the ability to continue to increase council tax charges will be tested in future years.</p> <p>The 4 year medium term financial plan reflects our local 'best estimate' of future inflation rates and government grants and contributions.</p>

4.4. The current policy is to maintain general balances at a guideline level of between 3% and 5% of annual net revenue expenditure budget.

- 4.5. It is recommended that the Commissioner agree a strategy to maintain a general reserve at a level between 3% and 5% of the revenue budget.
- 4.6. The level of general balances as at 31st March 2019 is forecast to be £10.175m (3.56% of the 2019/20 Revenue Budget).
- 4.7. Potential requirements to draw down from the general reserve in future years are monitored and reported to the Commissioner throughout the year and will be reflected in the annual review of the reserves strategy.

5. Earmarked Reserves

- 5.1. Reserves are also held to meet specific purposes, they are currently grouped together as "Earmarked Reserves"; they are included here to allow the full picture of financial risks covered to be considered alongside general reserves. The table below sets out the earmarked reserves held.

	31/3/18 £m	31/3/19 £m
<u>EARMARKED RESERVES</u>		
Reserves held for 'one-off' investment		
Transition Reserve	16.176	14.783
PCC Strategic Investment reserve	5.998	-
	22.174	14.783
Forensic Partnership reserve	0.406	0.181
Reserves held to support operational policing		
Protective Clothing Reserve	0.471	0.384
Vehicle Workshop Reserve	0.040	0.040
Wellbeing reserve	0.026	0.016
Operational Policing Reserve	0.364	2.003
	0.901	2.443
POCA Equalisation Reserve	0.640	0.547
POCA/Drugs Forfeiture Reserves	0.266	0.300
Road Safety Reserves	1.779	1.974
Regional collaboration	0	0.056
Total Earmarked Reserves	26.166	20.283
General Reserves	11.782	10.175

- 5.2. The Transition Reserve and the PCC Strategic Investment reserve are held to manage the transformation of the Constabulary and to support the Commissioner's capital programme through 'one-off' investments. These reserves have been created in recent

years through the early realisation of planned efficiency savings with a strategy to create reserves to enable investment that will continue to deliver programmes that provide further improvements in efficiency and productivity for the organisation.

- 5.3. The **Forensic Partnership Reserve** is held for investment in the delivery of the Forensics Partnership with UCLAN (University of Central Lancashire).
- 5.4. The **Operational Policing reserve** is held to meet unexpected and significant demand placed upon the force in any discrete financial year. Such demand might qualify for 'Special Grant' provided by the Home Office, however the rules for special grant require the force to meet the costs of such incidents up to an amount equivalent to 1% of their net revenue budget and then make a claim for any additional costs above this amount.
- 5.5. The **Protective Clothing Reserve** is set aside for specialist protective clothing for officers.
- 5.6. The **Wellbeing reserve** is set aside to support the constabulary well-being programme for all staff.
- 5.7. The **Vehicle Workshop reserve** is held for investment in the Vehicle Maintenance Unit (VMU) workshop specialist equipment.
- 5.8. **Police and Crime Act (POCA) reserves** are held for investment in Crime reduction schemes within the Communities of Lancashire and are created through the seizure of cash and assets on the conviction of criminals.
- 5.9. **Road Safety Reserves** are held on behalf of Lancashire Road Safety Partnership and are not available for use by the PCC. **Regional Collaboration reserve** is held in respect of the regional serious and organised crime team.
- 5.10. The current forecast of the application of these specific reserves in future years is set out in the table below:

Forecast application of reserves

<u>EARMARKED RESERVES</u>	Position 31/3/19	2019/20	2020/21	2021/22	2022/23	2023/24	Forecast position 31/3/24
	£m	£m	£m	£m	£m	£m	£m
Transition Reserve	14.783	-7.232	-4.478	-2.391	-0.682	0	0.0
Forensic Partnership reserve	0.181	-0.181	0	0	0	0	0.0
Protective Clothing Reserve	0.384	-0.050	-0.050	-0.050	-0.050	-0.050	0.134
POCA Equalisation Reserve	0.547	-0.100	-0.100	-0.100	-0.100	-0.100	0.047
POCA/Drugs Forfeiture Reserves	0.300	-0.100	0	-0.100	0	-0.100	0.0
Vehicle Workshop Reserve	0.040	0	0	0	0	0	0.040
Operational Policing Reserve	2.003	-1.003	-1.000	0	0	0	0.0
Well-being reserve	0.016	-0.016	0	0	0	0	0.0
Road Safety Reserves	2.030	-0.056	0	0	0	0	1.974
Total Earmarked Reserves	20.284	-8.738	-5.628	-2.641	-0.832	-0.250	2.195

5.11. The Home Office has set out guidance for the information to be provided in the PCC's reserve strategy. This guidance requires the classification of reserves held by the PCC as follows:

Funding for planned expenditure on projects and programmes over the period of the current medium term financial plan:	31/3/18	31/3/19
Earmarked reserves:	£m	£m
Transition reserve	16.176	14.783
PCC Strategic Investment Reserve	5.998	0
Forensic Partnership Reserve	0.406	0.181
	22.580	14.964

Funding for planned expenditure on projects and programmes beyond the period of the current medium term financial plan:	31/3/18	31/3/19
Earmarked reserves:	£m	£m
NIL	nil	nil

Resource to meet other expenditure needs in accordance with sound principles of good financial management	31/3/18	31/3/19
Earmarked reserves:	£m	£m
Protective Clothing Reserve	0.471	0.384
POCA Equalisation Reserve	0.640	0.547
POCA/Drugs forfeiture Reserve	0.266	0.300
Vehicle Workshop Reserve	0.040	0.040
Wellbeing reserve	0.026	0.016
Operational Policing Reserve	0.364	2.003
	1.781	3.274

General reserves	31/3/18	31/3/19
	£m	£m
General reserves	11.782	10.175

Reserves held on behalf of other organisations	£m	£m
Road Safety Reserves	1.779	1.974
Regional collaboration	-	0.056

5.12. The application of funding for the capital investment programme including the specific investment reserves shown in the table above is as follows.

	19/20	20/21	21/22	22/23	23/24	Total
	£m	£m	£m	£m	£m	£m
Capital Receipts	0.710	-	-	-	-	0.710
Capital grant	1.342	1.100	1.100	1.100	1.100	5.742
Revenue	1.717	2.650	3.650	4.650	4.650	17.317
Reserves	7.232	4.478	2.391	0.682	0	14.783
Borrowing	14.965	17.672	17.390	4.700	0.940	55.667
Financing to be identified	0	0	0	1.813	6.507	8.320
TOTAL	25.966	25.900	24.531	12.945	13.197	102.539

Further detailed analysis of the funding of the programme is shown at Annex 1.

5.13. It is recommended that the Commissioner approve the application of specific reserves as set out in the table above and in Annex 1.

5.14. From this forecast it is clear that the specific reserves will be used by 2022/23. The Commissioner and Chief Constable will consider alternative sources of funding to meet the financing gap identified in 2022/23 and 2023/24.

5.15. As specific reserves are limited it is recommended that the Commissioner review the reserves strategy on an annual basis.

5.16. It is recommended that the Commissioner agrees to make contributions into specific reserves if the opportunity arises.

6. Risks

6.1. The inability to maintain an adequate general reserve to cover future uncertainties puts the PCC and Force at risk of government sanction and intervention.

6.2. The amount of funding for future years' capital programme will be significantly reduced as reserves are utilised and alternative investment strategies will need to be developed.

Capital Investment Programme - Financing

	19/20	20/21	21/22	22/23	23/24	Total
	£m	£m	£m	£m	£m	£m
Capital receipts:						
Accommodation schemes	0.710					0.710
Capital Grants and contributions:						
IT Systems replacement and development	0.242					0.242
Vehicle replacement programme	1.100	1.100	1.100	1.100	1.100	5.500
Capital grants and contributions	1.342	1.100	1.100	1.100	1.100	5.742
Borrowing:						
Custody suites	0.094	1.316	1.034	0	0	2.444
HQ rationalisation	4.606	0.940	1.222	0	0	6.768
Pendle	2.820	3.196	0	0	0	6.016
Skelmersdale	3.572	0	0	0	0	3.572
Greenbank	0.846	4.230	3.948	0	0	9.024
Occupational Health	1.504	0	0	0	0	1.504
Operating bases refurbishment	0	3.760	3.760	3.760	0	11.280
Public order facility	0	3.290	3.760	0	0	7.050
South Comms	0	0	2.726	0	0	2.726
Minor works	0.940	0.940	0.940	0.940	0.940	4.700
Contact centre	0.583	0	0	0	0	0.583
Borrowing	14.965	17.672	17.390	4.700	0.940	55.667
Revenue and reserves:						
Network and Security	0.650	0.683	0.717	0.753	0.790	3.593
Device upgrade and replacement	1.890	1.620	1.652	0.765	0.730	6.657
Systems replacement and development	2.863	1.175	0.835	3.090	5.540	13.503
Accommodation	0.208	1.128	1.110	0.300	0.060	2.806
Other capital schemes	1.138	0.622	0.427	0.437	1.037	3.661
Vehicle replacement programme	2.200	1.900	1.300	1.800	3.000	10.200
Revenue and reserves	8.949	7.128	6.041	7.145	11.157	40.420
<i>Revenue Contribution</i>	<i>1.717</i>	<i>2.650</i>	<i>3.650</i>	<i>4.650</i>	<i>4.650</i>	<i>17.317</i>
<i>Reserves</i>	<i>7.232</i>	<i>4.478</i>	<i>2.391</i>	<i>0.682</i>	<i>0</i>	<i>14.783</i>
	8.949	7.128	6.041	5.332	4.650	32.100

The 2018/19 Capital Investment Programme was approved in this decision by the Commissioner:
<http://lancashire-pcc.gov.uk/wp-content/uploads/2018/02/2017-49.pdf>