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SURREY POLICE

PAPER FOR POLICE AND CRIME COMMISSIONER

Date: 22/07/15

ANNUAL UPDATE OF SURREY GENERAL AND SPECIFIC RESERVES STRATEGY

1. Purpose

1.1.The purpose of this report is to provide an update to the Reserves Strategy for agreement by the Police and Crime Commissioner with advice from the Treasurer. All reserves are under the control and preserve of the Police and Crime Commissioner (PCC) and will remain so subject to some flexibility previously agreed in respect of specific reserves.

2. Introduction

2.1.This paper updates the General Reserves Strategy which was last approved by the PCC in 2014. The paper sets out the use of general and specific reserves (i.e. earmarked revenue reserves) the latter which are by their very nature, reserves which have been earmarked for a specific purpose. The strategy on general and specific reserves forms part of the Medium Term Financial Plan which is updated regularly and reviewed by COG / SLT and the PCC. This paper requests approval of the use of general reserves over the planning period.

2.2.In preparing this review of the General Reserves Strategy we have reviewed the legislative and other requirements for the holding of reserves. We have also looked at the Force's current financial position, at current and future risk assessments and at updated benchmarking information on reserve levels in other Forces by the national Audit Office. We have taken account of the views expressed by the Office of the PCC and considered public opinion, and the reserves levels set out as part of the budget agreed by the PCC for 2015/16 and for the forthcoming four year period. Finally we have taken account of the reduction in central grant and limiting of precept increases over the planning period.

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

3.1.Legislation and CIPFA guidance 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 PCCs Treasurer) to report on the level of reserves annually, the planned usage and the opportunity cost of holding those reserves.

3.2.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."

3.3.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."

4. Factors to consider in deciding on reserve levels

4.1. Overall financial position and adequacy of financial control

- 4.1.1. In setting the level of the general reserve it is important to bear in mind Surrey Police's overall financial position and the adequacy of financial control in operation.
- 4.1.2. 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 public sector deficit reduction.
- 4.1.3. It is also important to remember the context of the medium term financial plan 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".
- 4.1.4. The use of general reserves does afford the PCC some flexibility in managing the budget over a number of years and there is merit in using reserves in the short term that is backed by a plan to restore those reserves to a set agreed level. For example half a percentage point affords £1m of budget flexibility to the PCC.

4.2. Risk exposure and risk assessment

- 4.2.1. 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 Force."
- 4.2.2. 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.
- 4.2.3. The key risks currently relevant to the level of general reserves now and in the future are;
 - 4.2.3.1. Future Funding Gap – the risk that due to the economic conditions, and real terms reductions in levels of precept and notified reductions in government grant, the increased resource requirements will have a significant effect on already stretched financial resources. These additional requirements may include funding increased contributions for pension schemes, a huge programme of change, including collaboration, to achieve a sustainable financial position. 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.
 - 4.2.3.2. Uncertain central funding after 2015/16 due to impending funding formula review, most likely to be in place for 2016/17 and the continuing commentary from government of further reductions in funding for the non-protected services.
 - 4.2.3.3. The use of "top slicing" by government introduces another unknown and increases uncertainty over the level of funding forces will have in future years.
 - 4.2.3.4. The potential for government control of precept increases through the capping regime. Recent years this has been set at no more than 2% with some ministers wishing for that to be lowered.

4.3. Public opinion

- 4.3.1. 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 Op Franklin response to severe weather conditions, it is likely that the public would expect the organisation to have sufficient resources to cover the expense without recourse to overspend.

4.4. Other police forces reserve levels

4.4.1. The National audit Office published a report in June 2015 that detailed the level of reserves held by Forces as at the end of 2013/14, the total of general and specific reserves as a percentage of the revenue budget ranged from 9% to 38% with Surrey at 15%; see appendix 1 for the chart.

4.4.2. Of the 41 Forces within the chart Surrey are 28th (with the first having the largest ratio). From previous surveys Surrey had been about mid table which suggest Forces have increased their reserves to a greater extent.

4.4.3. The above survey, Home Office and other commentators have led to a belief that the level of reserves by some in Policing and Local Authorities can be used as a means by the government to meet their austerity targets even though no specific information is available at this time. There was no information in the Chancellor's July 2015 Budget that shed any light on this possibility other than reference to the Spending Review this autumn. This is considered a risk as the Force's plans to employ reserves could be disrupted by any initiative from central government to rely on our reserves.

5. Current general reserve levels and their use

5.1. Use of General Reserves

5.1.1. The current strategy for general reserves levels is 3% of the annual revenue budget which is from considering the above factors and that 2% is considered a reasonable level for local authorities with an additional 1% for an emergency service to cater for the operational risks.

5.1.2. The use of general reserves assists in the medium term financial planning to mitigate any predicted funding gaps noting that this is a measure that allows a re-phasing of the gap and not a permanent reduction in the base budget.

5.1.3. 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.

5.1.4. The general reserve may also be used to fund capital investment.

5.2. The level of a General Reserve is a matter for the Police and Crime Commissioner as advised by his Treasurer (CFO). The strategy previously agreed is to maintain general reserves at 3% of budget.

5.3. The forecast level of reserves as at the 31 March 2016 is £11.4m which is 5.5% of the gross budget; this is after the uplift in reserves due to the collection fund surplus and tax base increase being greater than planned. The forecast position on reserves until 2019/20 is detailed at appendix 2.

5.4. As part of the medium term financial plan the PCC and Chief Constable have agreed to draw on reserves to mitigate service delivery impact of the forthcoming reductions. The plan has £6.4m being used to meet budget support over the next four years.

5.5. The PCC has also made payments to assist with the police staff pension fund deficit. This payment and the above budget support may result in the general reserves level going below 3% which has been supported by the PCC. Our past experience shows that the Force will invariably under spend in each year by a modest amount and that the assumption of an under spend of £0.5m each year will maintain general reserves above the 3% strategy level. However noting the number of financial and operational risks present and the under spending not materialising,

approval from the PCC is sought to keep to the use of general reserves in the MTFP and for the reserves level to go below 3% with a subsequent plan to replenish back to 3%.

- 5.6.**The Force has during the 2015/16 budget process had agreed two new reserves funded from general reserves for Training £1m and Estate Improvement £0.5m.
- 5.7.**The use of reserves is a valuable tool to manage cost pressures over more than one year and as issues arise we should be flexible in their creation. A specific example is the significant project the Force is currently embarked upon to deliver a Joint ERP System across two Forces, the financials for which are beginning to surface.

6. Specific Reserves

- 6.1.**Reserves are also held to meet specific purposes, they are currently grouped together as “Specific 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 specific reserves held.

Specific Reserves		
	As at 1 April 2015	£m
1	Chief Constable Operational Reserve	1.0
2	Operation Heather Reserve	1.3
3	Insurance Self Fund Reserve	3.7
4	Police Officer Ill Health Reserve	2.0
5	Estate Maintenance Reserve	0.5
6	Training Reserve	1.0
	Total	9.5

- 6.2.**From the descriptions below it can be seen that the top two specific reserves are to meet operational issues and are available to the Chief Constable. A retrospective report to be submitted to the PCC when the reserve is employed.
- 6.3.**The next two are in place to manage day to day activity and with the PCC maintaining ownership and oversight it is proposed that the Force are permitted to continue managing these reserves in conjunction with advice from the Treasurer.
- 6.4.**The last two were approved in the last budget setting round to meet specific demands. An expenditure plan to be provided to the PCC to access these reserves.
 - 6.4.1.Chief Constable Operational reserve was established to allow any operational demands to be met without recourse to the PCC in line with the Home Office Guidance on financial Management.
 - 6.4.2.Operation Heather; established to meet the one off costs of an enquiry and inquests into a historical case.
 - 6.4.3.Insurance Self Fund Reserve is a fund to meet anticipated future claims and liabilities that have not crystallised as yet. This amount is reviewed annually by insurance actuaries.
 - 6.4.4.Police Officer Ill Health Reserve is maintained to meet the capital charge made by the Home Office for each officer that retires due to ill health. A percentage of the police officer cost as recommended by the Home Office is added to this reserve and the level will fluctuate from year to year depending on the number of retirees.
 - 6.4.5.Estate Maintenance; established to meet the cost of estate improvements.
 - 6.4.6.Training Reserve; this is to meet the cost of training officers in a range of skills so they are equipped to support the new policing model in development.

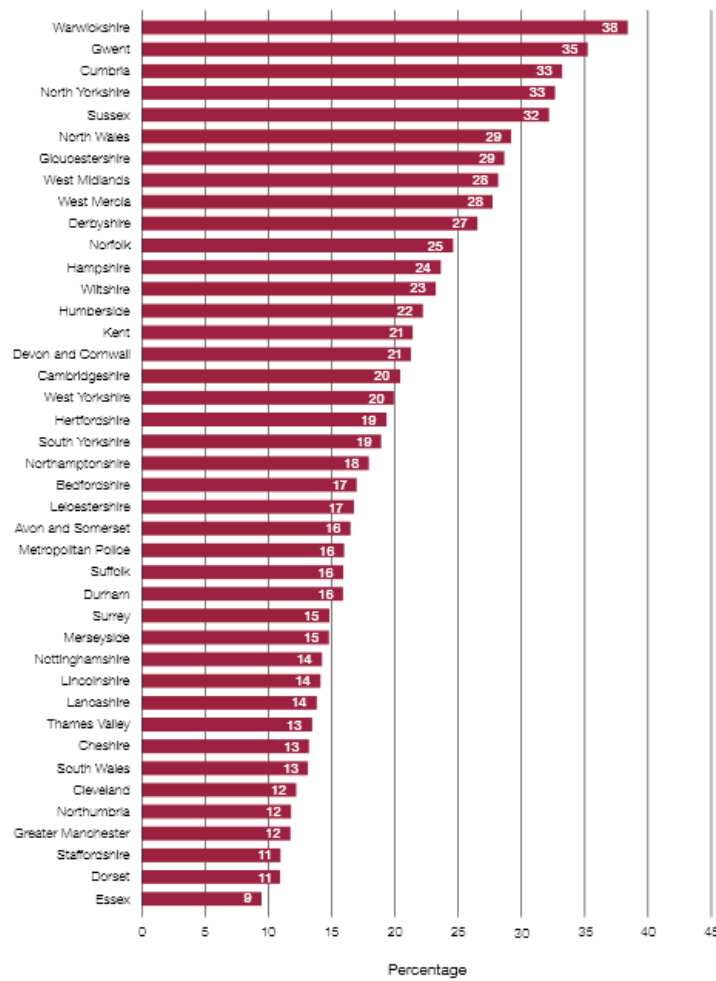
7. Risks

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

8. Decision[s] Required

- 8.1.**The level of a **General Reserve** is a matter for the Police and Crime Commissioner as advised by his Treasurer (CFO). The recommendation is to maintain the general reserve strategy at 3% of the annual revenue budget and move to that position over the next four years.
- 8.2.**Approve the use of general reserves to support the budget over the next four years in line with the approved medium term financial plan. (See appendix 2).
- 8.3.**Approval to allow general reserves, if required, to fall below 3% of the budget in order to maintain the use of general reserves as set out in the medium term financial plan.
- 8.4.**Approve the stipulations applied to specific reserves as detailed at 6.2 to 6.4.

Figure 14
Total earmarked and general reserves as a percentage of net revenue expenditure, 2013-14



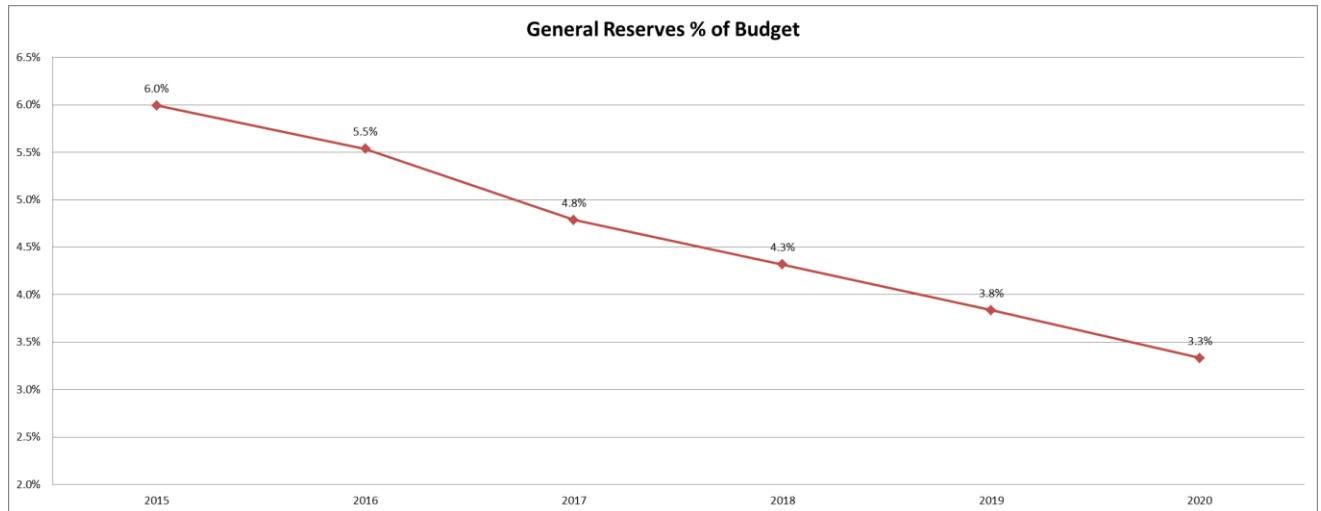
Notes

- 1 Excludes City of London and Dyfed-Powys forces owing to a lack of comparable data.
- 2 Each force will have their own reserves strategy with some reserves earmarked for investment, for example in estates or ICT. Some forces will also have reserves related to private finance initiatives.

Source: National Audit Office analysis of Chartered Institute for Public Finance and Accountancy data, available at: www.oipfastats.net/

Appendix 2

Surrey Police Reserves Estimates up to 2019/20



*estimated	31/03/2015	31/03/2016	31/03/2017	31/03/2018	31/03/2019	31/03/2020
	£m	£m*	£m*	£m*	£m*	£m*
General balances b/f	11.1	12.4	11.4	9.9	8.9	7.9
Budget Support	1.3	2.3	-2.0	-1.5	-1.5	-1.4
Other Additions	0.5	1.2				
Police Staff Pension Fund		-3.5				
Other Reductions	-2.3	-1.5				
Budget Under/Over Spend	1.8	0.5	0.5	0.5	0.5	0.5
General balances c/f	12.4	11.4	9.9	8.9	7.9	7.0
<u>Earmarked reserves</u>						
Chief Constable Operational Reserve	1.0	1.0	1.0	1.0	1.0	1.0
Local reserves	0.0	0.0	0.0	0.0	0.0	0.0
Insurance reserve	3.7	3.7	3.7	3.7	3.7	3.7
Police pension reserve	2.0	2.0	2.0	2.0	2.0	2.0
Health Care reserve	0.3					
Employee Retention Reserve	0.9					
Police Staff Pension Reserve	1.1	0.0	0.0	0.0	0.0	0.0
Training Reserve		1.0				
Estate Maintenance Reserve		0.5				
Operation Heather Reserve	1.3	1.3	0.0	0.0	0.0	0.0
Total Earmarked	10.3	9.5	6.7	6.7	6.7	6.7
TOTAL	22.7	20.9	16.6	15.6	14.6	13.7