

RESERVES STRATEGY

RESERVES, BALANCES AND PROVISIONS

1 Introduction

- 1.1. The requirement for financial reserves is acknowledged in statute. Sections 32 and 43 of the Local Government Finance Act 1992 which require local authorities in England and Wales to have regard to the level of reserves needed for meeting estimated future expenditure when calculating their budget requirement.
- 1.2. The Financial Management Code of Practice states that the Police and Crime Commissioner (Commissioner) should establish a strategy on reserves (including how they might be used by the Chief Constable) and provisions in consultation with the Chief Constable. This should have due regard to the need to ensure the on-going funding of policing activities and the requirement to meet exceptional or extraordinary policing operations.
- 1.3. Reserves are an essential part of financial management. They help the Commissioner and Chief Constable cope with unpredictable financial pressures and plan for future spending commitments.
- 1.4. All reserves will be held by the Commissioner and managed to balance funding and spending priorities and to manage risks. This forms an integral part of the medium-term financial planning process.

2. Definitions

- 2.1. Reserves and balances are different from provisions from an accounting perspective. In the case of useable reserves (as opposed to unusable reserves) and provisions, both amounts represented on the balance sheet should be matched by physical cash balances, unless internal borrowing has taken place.
- 2.2. **Usable Reserves** – are balances which are generally held for three specific purposes and are categorised as general reserves or earmarked reserves:
 - A working balance to help smooth the impact of uneven cash flows – general reserves;
 - A contingency to deal with unexpected events – general reserves;
 - A means of building up funds to meet known or predicted requirements – earmarked reserves.
- 2.3. **Earmarked Reserves** – these are balances that are being held by the for a specific initiatives and purposes.

- 2.4. **Ring-fenced Reserves** - these are balances that are being held by the Commissioner on behalf of third parties and cannot therefore be utilised without specific direction.
- 2.5. **Unusable Reserves** - do not have equivalent cash balances and are held for accounting purposes.
- 2.6. **Provisions** – are required for any liabilities of uncertain timing or amount that have been incurred.

3. Governance Arrangements

- 3.1. Minimum governance requirements in respect of reserves and balances are:
 - The Commissioner has a soundly based strategy on the level and nature of reserves and balances it needs which will be considered by the Joint Audit Committee;
 - The required levels of reserves and balances should be reflected in the annual budget and Medium Term Financial Plan (MTFP);
 - The Commissioner monitors and maintains the level of reserves and balances within the range determined by its agreed policy, advised by the CFO who will ensure that there are clear protocols for their establishment and use;
 - The Commissioner retains adequate reserves so that unexpected demand led pressures on budgets can be met without adverse impact on the achievement of the key priorities;
 - The Commissioner's strategy for reserves and balances is based on a thorough understanding of needs and risks, and is properly and clearly reported at the time the budget and precept are set. The level of balances is kept under review and managed to ensure that financial standing is sound and supports the Commissioner in the achievement of their long term objectives;
 - Where target levels for reserves and balances are exceeded, the opportunity costs of maintaining these levels has been established, compared to the benefit accrued.
- 3.2. Locally agreed Financial Regulations and the Scheme of Consent should:
 - Contain full details of how the Reserves and Balances strategy will operate locally;
 - Ensure that the annual budget includes a realistic amount of operational contingency that is available to the Chief Constable for operational priorities without the need for additional approval; and
 - Make provision, where appropriate, for budgets to be carried forward from one financial year to the next.

Statutory Responsibilities

- 3.3. The "CIPFA Statement on the Role of the Chief Finance Officer of the Police and Crime Commissioner and the Chief Finance Officer of the Chief Constable" sets out the five principles that define the core activities and behaviours that belong to the role of the CFO and the organisational arrangements needed to support them.
- 3.4. For each principle the Statement sets out the governance arrangements required within an organisation to ensure that CFOs are able to operate effectively and perform their core duties.
- 3.5. Governance arrangements required in respect of reserves and balances and which are the responsibility of the CFO are:
 - Ensuring that advice is provided on the levels of reserves and balances in line with good practice guidance;
 - To report at the time the budget is considered and the precept set, on the robustness of the budget estimates and the adequacy of financial reserves, as required by s25 of the Local Government Act 2003, and in line with CIPFA guidance.
- 3.6. Both should be undertaken in consultation with the Director of Finance (CFO Chief Constable).
- 3.7. There are also a range of safeguards in place that militate against the Commissioner over-committing financially. These include:
 - The balanced budget requirement;
 - Chief finance officers' Local Government Finance Act 1988 Section 114 powers which requires the chief finance officer to report if there is or is likely to be unlawful expenditure or an unbalanced budget; and
 - The external auditor's responsibility to review and report on financial standing includes a review of the level of reserves taking into account their knowledge of the organisation's performance over a period of time. However, it is not the responsibility of auditors to prescribe the optimum or minimum level of reserves for individual organisations.

5. Home Office Guidance on Police Reserves

- 5.1 On 31st March 2018 the Minister for Policing and the Fire Service published new guidance on the information that each PCC must publish in terms of police reserves.
- 5.2 One of the key requirements is that the information on each reserve should make clear how much of the funding falls into each of the following three categories:
 - Funding for planned expenditure on projects and programmes over the period of the current medium term financial plan
 - Funding for specific projects and programmes beyond the current planning period
 - As a general contingency to meet other expenditure needs held in accordance with sound principles of good financial management.

5.3 The Minister also outlined that future grant funding levels would take into account the transparent publication of this information across the service.

6. Assessing the Appropriate Level of Reserves

6.1 The Commissioner is responsible for ensuring that the level of reserves is appropriate for local circumstances, and is accountable to taxpayers for the decisions made. The CFO (PCC) has a duty to provide the Commissioner with the advice they need to make good decisions.

6.2 Reserves are maintained as a matter of prudence. They enable the organisation to provide for cash flow fluctuations and unexpected costly events and thereby help protect it from overspending the annual budget, should such events occur. Reserves for specific purposes may also be maintained where it is likely that a spending requirement will occur in the future.

6.3 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, it is likely that the public would expect that the organisation would have sufficient resources to cover the expense without recourse to overspend.

6.4 In order to assess the adequacy of reserves, the CFO (PCC) should include an up-to-date assessment of the strategic, operational and financial risks facing the organisations.

6.5 Setting the level of reserves is one of several related decisions that must be taken when preparing the MTFP and the budget for a particular financial year.

6.6 Assessing the required level of reserves should involve carrying out an analysis of the Balance Sheet on an annual basis and projecting forward the key items of the Balance Sheet. This projection incorporates forecasting levels of reserves and balances over a three year time horizon to cover the MTFP and capital programme.

6.7 In assessing the level of reserves due consideration is also taken of the Government support arrangements:

- Welsh Government Emergency Financial Assistance Scheme to help Forces faced with financial burden as a result of providing relief and carrying out immediate work in response to large scale emergencies. The scheme is subject to a threshold which is set at 0.2% of the revenue budget.
- Home Office Special Grant to meet additional costs that would be incurred from policing unexpected and exceptional events within their areas. If approved forces are expected to meet the additional costs of the event up to 1% of the revenue budget

6.8 An effective reserves and balances strategy should consider the organisations approach to treasury management, capital expenditure

plans and the need for external borrowing, against the use of balances and reserves.

- 6.9 CIPFA guidance suggests that in addition to cash flow requirements, the following factors should be considered:

Budget Assumptions	Financial Standing and Management
The treatment of inflation and interest rates	The overall financial standing of the organisations (level of borrowing, debt outstanding, council tax collection rates etc.)
Estimates of the level and timing of capital receipts	The organisations track record in budget and financial management including the robustness of the medium term plans.
The treatment of demand led pressures	The organisations capacity to manage in-year budget pressures
The treatment of planned efficiency savings/ productivity gains	The strength of the financial information and reporting arrangements
The financial risks inherent in any significant new funding partnerships, major outsourcing arrangements or major capital developments	The organisation's virement and end of year procedures in relation to budget under/over spends at organisational and departmental level
The availability of other funds to deal with major contingencies and the adequacy of provisions	The adequacy of the organisation's insurance arrangements to cover major unforeseen risks.

- 6.10 The Commissioner must have due regard to the need to ensure the ongoing funding of policing activities (including the requirement to meet exceptional or extraordinary operations). The annual budget should include a realistic amount of operational contingency to be available to the Chief Constable to meet operational priorities without the need for additional approval.
- 6.11 The Chief Constable will ensure that the annual revenue budget is sufficient to finance foreseeable operational needs by presenting a business case as part of the MTFP and annual budget setting process to the CFO (PCC) and Commissioner for one-off expenditure items to be funded from earmarked reserves.
- 6.12 The business case should include consideration of the level of reserves required for major incident investigations and other operational requirements, the amount of reserves required and timescales for their use.
- 6.13 Approval of business cases for the use of reserves will be subject to the authorisation limits set out in Financial Regulations, to assist with day to day operational decision making.

7. General Reserves

- 7.1 CIPFA's "Guidance Note on Local Authority Reserves and Balances" 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.*"
- 7.2 Whilst CIPFA does not stipulate a minimum or optimal level of general reserve, its general guidance is to establish a reserve representing "resources set aside for purposes such as general contingencies and cash flow management."
- 7.3 Setting the level of earmarked and general reserves is just one of several related decisions in the formulation of the MTFP and the budget for a particular year. Account should be taken of the key financial assumptions underpinning the budget alongside a consideration of the organisations financial management arrangements.

8. Earmarked Reserves including Ring-fenced Reserves

- 8.1 The current accounting Code requires the purpose, usage and basis of transactions of earmarked reserves to be clearly identified. A review of the purpose and level of reserves will be carried out annually during the budget setting process and details of the use of reserves included in the relevant note to the Statement of Accounts.
- 8.2 Earmarked reserves are categorised as either "usable" reserves or "unusable" reserves. Usable reserves can be applied to fund expenditure, unusable reserves are not resources backed and therefore do not have equivalent cash balances.
- 8.3 It is the Commissioner's policy to use reserves to fund non-recurring purchases to reduce the impact on the council tax precept. This includes using capital reserves to reduce the Capital Financing Requirement (CFR), if appropriate, which in turn will reduce the Minimum Revenue Provision charged to the revenue account annually.
- 8.4 The target level of earmarked reserves will therefore fluctuate annually but will always be justifiable and monitored to ensure levels of earmarked reserves are not too high or too low. Should the Commissioner deem that the level of usable reserves that he holds is above and beyond the levels reasonably required and specifically earmarked for future projects, the Commissioner may return reserves to the public. This is to be achieved by first utilising reserves to fund one off investments.
- 8.5 The reason useable reserves are held will be classified in line with the new Home Office classifications as outlined above.
- 8.6 Unusable reserves currently held include:
- **Revaluation Reserve** - The Revaluation Reserve contains the gains arising from increases in the value of Property, Plant and

Equipment and Intangible Assets. The balance is reduced when assets with accumulated gains are revalued downwards or impaired, consumed through depreciation, or disposed of and the gains are realised;

- **Capital Adjustment Account** - The Capital Adjustment Account absorbs the timing differences arising from the different arrangements for accounting for the consumption of non-current assets and for financing the acquisition, construction or enhancement of those assets under statutory provisions;
- **Accumulated Absences Account** - The Accumulated Absences Account absorbs the differences that would otherwise arise on the General Fund Balance from accruing for compensated absences earned but not taken in the year, e.g. annual leave entitlement carried forward at 31 March. Statutory arrangements require that the impact on the General Fund Balance is neutralised by transfers to or from the Account;
- **Pensions Reserve** - The Pensions Reserve absorbs the timing differences arising from the different arrangements for accounting for post-employment benefits and for funding benefits in accordance with statutory provisions.

9 Reporting Framework

9.1 The Commissioner has a fiduciary duty to local taxpayers and must be satisfied that the decisions taken on balances and reserves represent proper stewardship of public funds.

9.2 The level and utilisation of reserves will be informed by the advice and judgement of the CFO (PCC). To enable the Commissioner to reach their decision, the CFO (PCC) will report the factors that influenced their judgement and ensure that the advice given is recorded formally within the Medium Term Financial Plan. This report will include as a minimum a statement:

- detailing the level of general reserve and any movements on the fund;
- on the adequacy of the earmarked reserves, relative to spending and an estimate of provisions in respect of the forthcoming financial year and the MTFP;
- how reserves have changed over time;
- on the annual review of earmarked reserves including estimates of the year end balances. The statement will list the various reserves, their purpose, when they will be utilised and appropriate level; and
- An assessment of the risk of major incidents (operational and non-operational) occurring which is reflected in the budget and MTFP.

9.3 This report will be provided annually based on estimates to the Commissioner prior to approval of the council tax precept with the reserves position also being considered annually as part of the Commissioners approval of the Statement of Accounts.

9.4 As outlined above the Home Office issued specific guidance on Police Finance Reserves in January 2018 which seeks enhanced transparency across the service to demonstrate clear utilisation plans. The reporting framework detailed above addresses these requirements.

10 The "Opportunity Cost" of Holding Reserves

- 10.1 The external auditor encourages a statement within the Reserve Policy on the opportunity cost of holding reserves. "Opportunity Cost" is an economic theory term, which means if you spend something on one thing you cannot spend it on something else.
- 10.2 Applied to reserves, this means that if reserves are held which are too high, then an organisation is foregoing the opportunity to lower the Council Tax. This theory does not however lend itself well in practice where levels of council tax increase can be capped.
- 10.3 During the budget setting process the Commissioner considers using reserves for one off investments. This is considered a more sustainable use of 'excess' reserves and reduces the impact on the council tax precept. As reserves reduce the opportunity to do this reduces.
- 10.4 It is essential that the Commissioner's decisions on reserves are communicated clearly to local taxpayers to promote accountability.

11 Provisions

- 11.1 Provisions are required for any liabilities of uncertain timing or amount that have been incurred. Provisions are required to be recognised when:
 - the local authority has a present obligation (legal or constructive) as a result of a past event;
 - it is probable that a transfer of economic benefits will be required to settle the obligation; and
 - a reliable estimate can be made of the amount of the obligation.
- 11.2 A transfer of economic benefits or other event is regarded as probable if the event is more likely than not to occur. If these conditions are not met, no provision should be recognised.
- 11.3 The requirement for provisions will regularly assessed.

Appendix G– Reserves 2019/20 -2024/25

Revenue & Capital Reserves	Narrative Comment	Home Office Classification	Actual 31st March 2019	Estimated Reserves at 31st March 2020	Estimated Reserves at 31st March 2021	Estimated Balance at 31st March 2022	Estimated Reserves at 31st March 2023	Estimated Reserves at 31st March 2024	Estimated Reserves at 31st March 2025
		see below	£000k	£000k	£000k	£000k	£000k	£000k	£000k
General Reserves	The requirements of operational policing vary significantly from year to year. This General Reserve ensures that funds are available to respond to and mitigating the in year financial impacts of major incidents or unknown events. The PCC considers a number of factors in determining the level of reserves namely: Overall financial position and adequacy of financial control; Risk exposure and risk assessment; and Public opinion. This reserve which equates to 3.8% of the 19/20 revenue budget may also assist in mitigating any detrimental impact as a result of the Comprehensive Spending Review and changes to the police funding formula. Further information can be found within the published Reserves Strategy.	C	4,032	4,032	4,032	4,032	4,032	4,032	4,032
General Reserve as % of net revenue budget				3.77%	3.36%	3.23%	3.11%	2.99%	2.87%
Go Safe' Road Safety Partnership Reserve	This earmarked reserve is held on behalf of the all Wales 'Go Safe' Road Safety Partnership and will be utilised in line with their business requirements which may be beyond the life of the current planning period.	B	1,721	1,901	1,721	1,541	1,361	1,190	1,190
Regional Collaboration Reserve	This reserve represents the fair share of funds held for collaborative police services which include the Regional Organised Crime Unit and Regional Task Force. These funds will be utilised in line with business requirements to support operational delivery and subject to decisions by the Wales Collaboration Board may go beyond the life of the current planning period.	B	388	388	388	388	388	388	388
Total Ring-fenced Revenue Reserves			2,109	2,289	2,109	1,929	1,749	1,578	1,578
Earmarked Revenue Reserve	This reserve is being held to support the revenue budget over the next 3 years to mitigate future funding gaps and detrimental impact on service delivery as a direct result of the previous PCC's decision to reduce the council tax precept for 2015/16 by 5% and to utilise reserves to underpin the revenue budget.	A	1,336	723	224	-	-	-	-
Driver Retraining Scheme	This reserves is being held specifically to support activities in relation to road safety initiatives. Further opportunities will be explored to ensure that these reserves are utilised to optimal effect for the communities of Dyfed-Powys.	B	1,294	460	335	310	310	310	310
Proceeds of Crime Act	This reserve comes from funds which have been allocated to Dyfed-Powys as a result of confiscation orders arising from proceeds of crime. These reserves are then utilised to support operational activities which assist in bringing criminals to justice e.g. financial investigators.	A	218	210	151	92	33	33	33
Chief Constable Operational Fund	This is a new reserve being established to assist in mitigating against the consequential costs of notable peaks in operational activity.	A	386	485	485	485	485	485	485
Sustainability & Transformation Fund	This is a new reserve being established to assist in funding invest to save, sustainability and transformational initiatives.	A	494	494	324	154	-	-	-
Drug Intervention	This reserve will be utilised to support drug testing.	A	135	95	55	15	15	15	15
Total Earmarked Revenue Reserves			3,863	2,467	1,574	1,056	843	843	843

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		see below	£000k	£000k	£000k	£000k	£000k	£000k	£000k
Capital Grants	These capital grants are held to specifically support IT projects within the capital programme	A	425	183	-	-	-	-	-
Capital Reserve	This reserve will be utilised to support the significant capital investment in Estates, Information Technology and Fleet including a new custody and station facility within Carmarthenshire, providing a solution to ageing police facility in Brecon and will support a range of both national and local technological developments.	A	5,786	4,203	41	9	9	9	9
Total Capital Reserves			6,211	4,386	41	9	9	9	9
Total Reserves			16,215	13,174	7,756	7,026	6,633	6,462	6,462
Home Office Police Finance Res	Classifications								
Funding for planned expenditure on projects and programmes over the period of the current medium term financial plan	A								
Funding for specific projects and programmes beyond the current planning period	B								
A general contingency or resource to meet other expenditure needs held in accordance with sound principles of good financial management	C								
Classifications as outlined in the Home Office guidance on Police Finance Reserves which was issued on the 31st January 2018									
How reserves support the priorities of the Police & Crime Plan		General Reserve	Capital Reserve						
Keeping our communities safe		✓	✓						
Safeguarding the vulnerable		✓	✓						
Protecting our communities from serious threat		✓	✓						
Connecting with communities			✓						

