



# **Reserves Strategy**

**2010-2013**

# Contents

<b>Summary</b>	<b>3</b>
<b>1. Types of Reserves</b>	<b>4</b>
<b>2. General Reserves</b>	<b>7</b>
<b>3. Earmarked Reserves</b>	<b>13</b>
<b>4. Capital Reserves</b>	<b>19</b>
<b>5. Conclusion</b>	<b>20</b>
 <b>Background Papers</b>	 <b>21</b>
 <b>Annex A ~ Role for the CFO</b>	 <b>22</b>

## Executive Summary

Cheshire East Council will maintain reserves for two main purposes:

- 1. to protect against risk, and;**
- 2. to support investment**

The Reserves Strategy presents information about the requirements to maintain adequate financial reserves and provides statements on the types of reserves and current and predicted balances.

This strategy sets out a clear purpose for the holding of reserves, using risk assessments and setting out principles for the management of balances for the period 2010 – 2013.

The report follows guidance issued by the Chartered Institute of Public Finance & Accountancy ~ *LAAP Bulletin 55 – February 2003: Guidance Note on Local Authority Reserves and Balances*. Compliance with the guidance is recommended in the Institute's 2003 Statement on the Role of the Finance Director in Local Government and the regulatory framework and role of the Chief Finance Officer are set out in **Annex A**.

The opening balances for Cheshire East Council reserves come from the information supplied on the balance sheets of the 4 predecessor local authorities in Cheshire east area. It is important to recognise that, although the overall total of the former Cheshire County Council reserves will not change, the allocation between Cheshire East and Cheshire West & Chester is still subject to ongoing review.

This strategy represents the latest position, following further review of the balances previously held, to ensure they meet the needs of Cheshire East Council.

*Lisa Quinn*

Borough Treasurer & Head of Assets  
Cheshire East Council

# 1. Introduction

## Types of Reserves

1. When reviewing medium term financial plans and preparing annual budgets the Council must consider the establishment and maintenance of reserves. Two types of Revenue Reserves will be held:

### General Reserves (see Section 2)

This represents the non-ringfenced balance of Council funds. There are two main purposes to general reserves: firstly to operate as a **working balance** to help manage the impact of uneven cash flows and avoid unnecessary temporary borrowing, and; secondly to provide a **contingency** to cushion the impact of emerging events or genuine emergencies. The level of reserves retained will be risk based. General Reserves must be adequate and will increase and decrease as follows:

#### Increasing General Reserves

- *Planned repayment* as set-out in the budgeting process, usually to recover to an adequate level in relation to a detailed risk assessment, or to prepare in advance for future risks
- Allocation of an *operating surplus* at the close of the financial year

#### Decreasing General Reserves

- *Planned draw-down* of reserves to create investment, and to counteract the possibility of over-taxing in any financial year
- Allocation of an *operating deficit* at the close of the financial year

### Earmarked Reserves (see Section 3)

This provides a means of building up funds, for use in a later financial year, to meet known or predicted policy initiatives. Discipline is required around setting up and maintaining earmarked reserves, and this strategy sets out the Council's approach to this. Earmarked reserves will increase through decisions of the Council and will decrease as they are spent on specific intended purposes.

## Assessing the Adequacy of Reserves

2. In order to assess the adequacy of unallocated general reserves when setting the budget, the Borough Treasurer will take account of the strategic, operational and financial risks facing the Authority. The Council will therefore adopt formal risk management processes. The Audit Commission Codes of Audit Practice make it clear that it is the responsibility of the audited body to identify and address its operational and financial risks, and to develop and implement proper arrangements to manage them, including adequate and effective systems of internal control. The financial risks will be assessed in the context of the Authority's overall approach to risk management.

3. There is now a requirement for local authorities to include an Annual Statement of Governance with the Statement of Accounts. The Chief Finance Officer will ensure that the Authority has put in place effective arrangements for internal audit of the control environment and systems of internal control, as required by professional standards.
4. Setting the level of general reserves is just one of several related decisions in the formulation of the medium term financial strategy and the budget for a particular year. Account will also be taken of the key financial assumptions underpinning the budget alongside a consideration of the Authority's financial management arrangements.
5. **Table 1** (below) sets out the significant budget assumptions that are relevant when considering the adequacy of reserves that are in addition to the issue of cashflow:

**Table 1: Holding adequate reserves will depend on a number of key factors**

Budget Assumptions	Financial Standing & Management
The treatment of inflation and interest rates	The overall financial standing of the Authority (level of borrowing, debt outstanding, council tax collection rates etc)
Estimates of the level and timing of capital receipts	The Authority's track record in budget and financial management including the robustness of the medium term plans
The treatment of demand led pressures	The Authority's 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 Authority's virement and end of year procedures in relation to budget under/overspends at authority and departmental level
The availability of other funds to deal with major contingencies and the adequacy of provisions	The adequacy of the Authority's insurance arrangements to cover major unforeseen risks

Source: CIPFA ~ LAAP Bulletin 55, 2003

6. These factors can only be assessed properly at local level. A considerable degree of professional judgment is required. The Borough Treasurer may choose to express advice on the level of balances in cash and/or as percentage of budget (to aid understanding) so long as that advice is tailored to the circumstances of the Authority for that particular year.

7. Advice will be set in the context of the Authority's Medium Term Financial Strategy and not focus on short term considerations, although balancing the annual budget by drawing on general reserves may be a legitimate short term option. However, where reserves are to be deployed to finance recurrent expenditure this should be made explicit, and will occur only to pump prime investment and not to regularly support such costs. Advice should be given on the adequacy of reserves over the lifetime of the Medium Term Financial Strategy.
8. The current guidance requires the purpose, usage and the basis of transactions of earmarked reserves to be identified clearly. A review of the levels of earmarked reserves will be undertaken as part of annual budget preparation.
9. Capital reserves will be maintained as part of the Capital Strategy monitoring and review. Such balances will inform decisions on borrowing and general management of the capital programme.

## 2. General Fund Reserves (Revenue)

### Purpose

10. The purpose of general reserves is to minimise the possible financial impacts to the Authority from:
- Emergencies;
  - In-year emerging issues;
11. Finance Procedure Rules allows the use of general reserves, with the following limitations:
- a. Estimates for unfunded use of reserves must be approved by Council
  - b. Fully funded estimates may be approved as follows:
    - Up to £0.1m Chief Officers
    - £0.1m to £0.5m Chief Officers in consultation with Cabinet Member and Cabinet Member for Resources
    - £0.5m to £1m Cabinet
    - Over £1m Council
12. The in-year use of general reserves requires Council approval and must not be used for any level of recurring spending, unless that spending will be included in revenues budgets in the following financial year or a suitable payback period is agreed in advance.
13. In all cases the use of reserves should be approved by the Borough Treasurer.

### Opening Balances

14. At 1<sup>st</sup> April 2010, Cheshire East Council is anticipated to hold general reserves of £17.565m. This balance takes account of sums transferred from predecessor authorities, approved contributions from earmarked reserves and unbudgeted income in 2009/2010, offset by approved contributions to earmarked reserves (eg Invest to Save) and approved schemes, and estimated costs of voluntary redundancy and transitional costs during 2009/2010. This can be summarised as shown in **Table 2** overleaf.

**Table 2: Transforming services during 2009/2010 is causing a reduction in general reserves**

Detail of Movements	£000	£000
<b>Estimated Opening General Reserves at 1st April 2009</b>		<b>24,449</b>
<b>Increases in Reserves</b>		
Transfer from Earmarked and Capital Reserves	5,219	
Unbudgeted Income (incl VAT reclaim)	4,189	
<b>Decreases in Reserves</b>		
Schemes approved in year	(2,039)	
Transfers to Earmarked Reserves :		
Invest to Save & other items	(2,753)	
Voluntary Redundancy costs	(11,500)	
<b>Net Changes in 2009/2010</b>		<b>(6,884)</b>
<b>Estimated Closing Balance at 31st March 2010</b>		<b>17,565</b>

Source: Cheshire East Finance - February 2010

15. The following principles are adopted for Voluntary Redundancy and other Transitional costs:

- Significant levels of Voluntary Redundancy payments are being met centrally, including all associated severance costs.
- Where one-off severance costs are paid centrally, then the actuarial costs are also allowed for centrally. This supports the corporate commitment to invest in service transformation.
- Actuarial costs should be recovered from reserves or from services over three years (although in cash terms they will be paid over 5 years).
- Only relocation costs incurred by ex Cheshire County Council staff now travelling from West to East will be met from reserves. All other disturbance costs are to be met from services.

16. The opening balance reflects current estimates and it is important to note that there is still some scope for amendments, following final agreement on disaggregation of the County Council balance sheet, so figures are still provisional at this stage.

### **Estimated Movement in Reserves (2010/2011 onwards)**

17. **Table 3** (overleaf) summarises the current estimated movements in general reserves from 2010 to 2013. This position makes a clear assumption that any



recently identified in-year, or future, emerging financial pressures will be met from within the Council's funding envelope.

18. In addition the level of reserves needed will be assessed each year according to the risks facing the Authority (see Risk Assessment below).

**Table 3: Reserves should remain higher than the 'Risk Assessed Minimum Level'**

Detail	2010/11 £000	2011/12 £000	2012/13 £000
<b>Estimated Balance @ 1<sup>st</sup> April</b>	<b>17,565</b>	<b>21,273</b>	<b>26,653</b>
<b>Projected Increases in Reserves</b>			
- Contingent Asset (VAT reclaim) net of fees	600		
- Business Finance Loan Repayments	278	146	
- Contribution from Earmarked Reserves	42	42	
- Planned Contribution to Reserves	4,288	5,192	6,063
<b>Projected Use of Reserves</b>			
- Impact of Transitional & Voluntary Redundancy Costs (transferred to earmarked reserves)	-1,500		
<b>Forecast General Reserves @ 31<sup>st</sup> March</b>	<b>21,273</b>	<b>26,653</b>	<b>32,716</b>
Risk Assessed Minimum Level	20,579		
<b>Un-Allocated Balance</b>	<b>694</b>		

Source: Cheshire East Finance ~ February 2010

19. Transitional costs, from local government reorganisation, have been met from general reserves, and by making a contribution from revenue income each year those reserves will be replaced. The reserves position for 2010/2011, as detailed in **Table 3** (above), reflects the aim of Cheshire East Council to repay Transitional Costs and Voluntary Redundancy costs over the three-year planning period.

### **General Fund Reserves - Risk Assessment**

20. Local Authorities have often adopted a broad principle that General Fund Reserves would be prudent if equivalent to 5% of the net revenue budget requirement. However, the risks facing each local area will vary, and in the case of Cheshire East, the recent impact of reorganisation combined with the economic climate and pressure on public services still presents the potential for significant emerging risk.
21. The desired level of reserves is therefore substantiated by a detailed risk assessment. This approach allows the Council to take account of the circumstances around current structural changes and economic circumstances.
22. Where specific financial liability has not been established, or where outcomes from emerging pressures cannot be detailed, the Council will assume a level of

risk. This reduces the possibility that the Council will be exposed to financial pressure and smoothes the impact on citizens.

23. Risks are categorised, and potential values are applied to them, this presents the potential exposure to financial risk. **Table 4** (below) shows the risk areas and the level of reserves the Council should retain to mitigate that risk. In each case the value of the risk retained has been calculated as a % of the potential impact. The % is based on the likelihood of the risk actually achieving that total impact.

24. It is possible that a number of events could happen in a single year. It is also possible that the Council could be exposed to new unidentified risks. For this reason the analysis also contains a Strategic Reserve calculated as a % of the net revenue budget.

25. Risks will be included and managed using the following basic principles:

- a. The risk may impact within the medium term
- b. Risks are potential one-off events
- c. The risk will have genuine financial consequences
- d. Mitigating actions will be in place to minimise the potential requirement for financial support
- e. If a risk becomes 100% likely it should be allocated to earmarked reserves
- f. Emerging risks will be addressed from in-year surplus or virement before any request to allocate general reserves

**Table 4: A robust level of reserves is guided by an assessment of potential risks**

Class of Risk	Knock on Effects	Effect on budget / Mitigating action	Value of risk retained
<b>Health &amp; Safety</b>	Major loss of service	Increased cost to reduce further risk of breach / Robust risk assessments	£100,000
	Loss of income	Substantial disruption to income streams / Robust disaster recovery	£50,000
	Lost reputation	Cost of new advertising to regain confidence / Effective Communication Plans	£10,000
	Effect on recruitment	Additional advertising costs to attract staff / Employment options on standby	£20,000
<b>Fire / Structural damage by flood etc</b>	Major loss of service	Premises not operational / Robust disaster recovery plan	£100,000
	Epidemic	High staff sickness & absence costs / raise awareness of safety measures and introduce robust emergent response plans	£304,000
	Severe Weather	Additional staffing, transport and materials costs / robust emergency plans	£150,000
Class of Risk	Knock on Effects	Effect on budget / Mitigating action	Value of risk retained

	Insurance claims create rising premiums or cost to insurance reserves	Budget growth to cover premiums or self insurance costs / Good claims management	£25,000
<b>Budget Pressures</b>	Efficiency savings challenged by changing priorities, and reduced income from economic downturn	Impact of 2009/2010 projected outturn / Robust remedial plans and monitoring of progress	£5,120,000
	Disaggregated Balances vary from current predictions	Impact on opening balances / apply prudent assumptions to opening balances	£2,500,000
	Income from fees and charges affected by economic downturn	Loss of income from fees & charges from local economic pressures / prudent income targets; close monitoring	£550,000
	Higher than anticipated inflation arising in year	Increased inflation on contracts and services / contract management and robust remedial plans	£1,200,000
	Efficiency savings challenged by changing priorities	In-Year emerging issues / Robust remedial plans and monitoring of progress	£2,400,000
<b>ICT &amp; Security</b>	Court Fine and need to improve security	Up to 10% fine on turnover / robust security processes	£250,000
	Data corruption	ICT service days to repair, loss of service / robust security policies and firewalls	£50,000
<b>Legal actions / Industrial relations / Failure of External organisations</b>	Disruption to service and/or costs of arbitration / tribunal / damages	Loss of income, costs of providing essential services or direct costs of resolution, reduced pay budget / emergency planning	£50,000
<b>Strategic Reserve</b>		Strategic/Emergency risk cover, potential further invest to save options and future pay structure changes	£7,700,000
<b>OVERALL RISKS</b>			<b>£20,579,000</b>
<b>% of Net Revenue Budget</b>			<b>8.6%</b>

Source: Cheshire East Finance Feb 2010

26. The outcome of this analysis has been to place an estimated total value on the range of risks that may arise and which are not covered by insurance. This is equivalent in total to £20.6m

27. It should be noted that these risks include significant sums relating to the final disaggregated balances position and the 2009/2010 outturn forecast, which if they should materialise would considerably reduce the actual general reserves position shown above (albeit that the risk would then be reduced also).

### Adequacy of General Reserves

28. A duty of the Chief Finance Officer is to comment on the adequacy of financial reserves (**see Annex A**).
29. The estimates contained within the Medium Term Financial Strategy must be sufficiently robust to achieve certainty that reserves are adequate. The Chief Finance Officer will comment specifically in the annual Budget report on the robustness of estimates and, therefore, the adequacy of reserves.

### 3. Earmarked Reserves (Revenue)

#### Purpose

30. The purpose of earmarked reserves is:

- a. To prevent an uneven impact from policy options, by allowing balances to be set aside for future year expenditure
- b. To set aside amounts for projects that extend beyond 1 year

31. Once Earmarked reserves have been established by Council it is the responsibility of Chief Officers, in consultation with the Borough Treasurer to ensure balances are spent in line with their purpose.

32. **Table 5** (below) identifies the most commonly established earmarked reserves and the rationale behind why such reserves are created and maintained.

**Table 5: All earmarked reserves should have a clear rationale**

Category of Earmarked Reserve	Rationale
Sums set aside for major schemes, such as capital developments or asset purchases, or to fund major reorganisations	Where expenditure is planned in future accounting periods, it is prudent to build up resources in advance
Insurance reserves	Self-insurance is a mechanism used by a number of local authorities
Reserves of trading and business units	Surpluses arising from in-house trading may be retained, or may have to be retained by statute to cover potential losses in future years, or to finance capital expenditure
Reserves retained for service departmental use	Increasingly authorities have internal protocols that permit year-end surpluses at departmental level to be carried forward
School Balances	These are unspent balances of budgets delegated to individual schools

Source: CIPFA ~ LAAP Bulletin 55, 2003

33. For each earmarked reserve held by Cheshire East Council there will be a clear protocol setting out:

- the purpose of the reserve
- how and when the reserve can be used
- procedures for the reserve's management and control
- a process and timescale for review of the reserve to ensure continuing relevance and adequacy
- clear indication of payback periods and approach (if applicable)

34. When establishing reserves, Cheshire East Council will ensure that it complies with the Code of Practice on Local Authority Accounting in the United Kingdom and in particular the need to distinguish between reserves and provisions.
35. The protocol for Cheshire East Council earmarked reserves is set out below. The Borough Treasurer will monitor adherence to these protocols. Details of each reserve will be held to demonstrate compliance with the protocols.
36. Earmarked Reserves will be:
- Set up by Full Council, on recommendation by the Borough Treasurer
  - Supported by a business case
  - Held for a maximum of 3 years, except where the business case justifies a longer retention.
  - Subject to a minimum value, set initially at £60,000 (unless business case supports lower level)
  - Be reviewed at least annually
37. Services may also carry forward balances strictly in accordance with Financial Procedure Rules.
38. At 1<sup>st</sup> April 2010 it is anticipated that the balances on existing earmarked reserves held by Cheshire East Council will be £9.9m. **Table 6** (overleaf) shows the position on each earmarked reserve. The approved balance at the last review of strategy in November 2009 takes account of opening balances from each contributing local authority, the impact of the decisions taken by Council on creating new earmarked reserves for Invest-to-Save projects, Local Area working and People into Jobs, and the return of £4.6m of earmarked balances into general reserves.
39. Earmarked Reserves have been further reviewed, and estimates made of the likely use of the reserves in 2009/2010. Reserves have also been aggregated where appropriate.
40. Earmarked reserves have the effect of transferring the tax burden across financial years as current taxpayers' funds are being used to support future years' spending. It is therefore recommended that the Council's earmarked reserves are subject to annual review, at least as part of the budget-setting process to ensure that they are still appropriate, relevant and adequate for the intended purpose.

**Table 6: Earmarked Reserves can pump prime initiatives that may deliver future savings**

Directorate / Description	Approved Revised Balance November 2009 £000	Estimated movement in 2009-10 £000	Estimated Opening Balance 1 April 2010 £000	Reason / Use
<b>PERFORMANCE &amp; CAPACITY</b>				
<b>Borough Treasurer</b>				
Invest-to-Save Projects	2,000	0	<b>2,000</b>	Central reserve to support invest-to-save projects
Insurance Reserve	737	597	<b>1,334</b>	To settle insurance claims
Interest Free Loans	242	-42	<b>200</b>	Full amount will be returned to General Reserves as debtor balances are paid
Deferred VR Payments	222	-222	<b>0</b>	To be paid in 2009/2010
Public Buildings repair & maintenance	210	0	<b>210</b>	£145,000 Condition Survey-led repairs, £65,000 General
Environmental Warranties	168	1,582	<b>1,750</b>	Self-insurance for possible claims from Cheshire Peaks and Plains, related to LSVT
Collection Fund Discretionary Relief	139	0	<b>139</b>	Balance used for discretionary relief on business rates
Commuted Community Sums	82	-82	<b>0</b>	Deferred Grants related to S.106 funding
Crewe Business Park - Marketing Office rent	46	-21	<b>25</b>	Approved for repairs / costs in the event of transfer of management of Park
Repairs/Renewals Fund	38	0	<b>38</b>	Outstanding payment due in 2009/2010
Benefits Appeals	0	400	<b>400</b>	Reinstatement of reserve to meet potential appeal costs
<b>HR &amp; OD</b>				
Job Evaluation	300	0	<b>300</b>	Intended to be used to offset final protected pay in 2009/2010
Single status/ job evaluation	186	0	<b>186</b>	Intended to be used to offset final protected pay in 2009/2010
<b>Policy &amp; Performance</b>				
Ward budgets	7	-7	<b>0</b>	Crewe Wards allocation for community spend in 2009/2010
Enabling Local Working	625	0	<b>625</b>	Available to promote local working
Partnerships & Grants Support	156	0	<b>156</b>	Funding issued to groups who meet the Council's criteria.

<b>Directorate / Description</b>	<b>Approved Revised Balance November 2009 £000</b>	<b>Estimated movement in 2009-10 £000</b>	<b>Estimated Opening Balance 1 April 2010 £000</b>	<b>Reason / Use</b>
Cheshire Community Action Grant Funding	67	-67	0	Allocated in 2009/2010 to support work in rural communities and the development of parish plans.
<b>PEOPLE</b>				
Children's – Extended Schools Services	573	-573	0	Underspent Area Based grant
Education All Risks	308	0	308	Carried forward surplus of premiums paid by schools ~ operated as a trading account
S117 Reserve	130	0	130	Based on Population
LPSA Reserve (continuation funding)	128	-128	0	Continuation Funding Improving Quality of life for older people, includes accrued funding for 2009/2014
Long Term Sickness	96	0	96	LTS Insurance Scheme, surplus premiums paid by schools ~ operated as a trading account
LPSA Reserve (continuation funding)	62	-62	0	Continuation Funding Employment opportunities for people with disabilities, includes accrued funding for 2009/2012
Part-time Rangers (H & W)	62	0	62	Earmarked for spending on additional hours for ranger service
LPSA Reserve (continuation funding)	43	0	43	Continuation Funding Increasing safety from domestic abuse, includes accrued funding for 2009/2015
Cumberland pitch renewal	30	0	30	Following major investment, using annual additional surplus to build a fund to renew in future
Leisure	124	-23	101	Various commitments, including premises repairs
Fluctuation in School Days	0	223	223	To meet annual changes in School transport costs due to varying dates of the Easter period
<b>PLACES</b>				
Economic Development Projects	842	-765	77	Various economic and business development projects
Economic Development	650	-650	0	Used in 2009/2010 for statutory and development requirements
Building Control	581	-250	331	Ring-fenced surplus (could be used to offset service deficit, if applicable)



<b>Directorate / Description</b>	<b>Approved Revised Balance November 2009 £000</b>	<b>Estimated movement in 2009-10 £000</b>	<b>Estimated Opening Balance 1 April 2010 £000</b>	<b>Reason / Use</b>
Town centre improvements	326	-326	0	Used to meet costs during Crewe town centre redevelopment
Crematoria	279	0	279	Investment in improved cremation facilities (funds built up via ringfenced income for mercury emissions abatement)
Local Development Framework	192	- 25	167	To manage peaks in LDF spending
Housing Stock Condition Survey	170	-50	120	Utilising part of the LPSA2 Performance Reward Grant
Markets	154	-25	129	Displacement of market during Lyceum Square development, and maintenance/improvement initiatives
People into Jobs	138	-138	0	Per Cabinet Report February 2009
Disturbance Payments	122	-50	72	Covering costs from relocation of staff due to office centralisation (also funding shuttle bus service)
Tatton Park	120	-20	100	Ring-fenced surplus on Tatton Park trading account
Community Safety	109	-109	0	To provide additional capacity in 2009/2010, which will enable invest to save options to be adapted for future years
Waste Management	105	-105	0	Contract delay and acquisition of plant/equipment
On-Street Parking	90	-90	0	Fund for repayment of set-up costs for DPE
Climate Change & Sustainability	85	-20	65	Continuation Funding creating sustainable communities
Queens Park Restoration Project	84	-20	64	Occupant relocation costs and contingency re project management/delivery
Footways & Street Lighting	78	-10	68	Continuation Funding tackling poor footways and street lighting
Safer Communities	74	-30	44	PCSOs/ ASB Co-ordinator commitments; maintenance of alley gates
Trading Standards	60	-60	0	To protect against possible shortfall in essential service during 2009-10

<b>Directorate / Description</b>	<b>Approved Revised Balance November 2009 £000</b>	<b>Estimated movement in 2009-10 £000</b>	<b>Estimated Opening Balance 1 April 2010 £000</b>	<b>Reason / Use</b>
Local Infrastructure Survey	52	-52	0	Survey of minor bridges, lighting etc to ascertain ownership / maintenance liability
Environmental Improvements	36	-36	0	Local Community led small environmental improvement projects
Community Wardens - Fixed penalties	34	0	34	Statutorily ring-fenced for improving cleanliness of public spaces
Places General Reserve	160	-160	0	Street Lighting and various minor reserves
<b>Totals</b>	<b>11,322</b>	<b>-1,416</b>	<b>9,906</b>	

Source: Cheshire East Finance review January 2010

## 4. Capital Reserves

41. The purpose of capital reserves is to:
  - a. Minimise risk from potential emergency spending requirements on assets
  - b. Support investment in tangible and intangible assets
  - c. Hold committed balances, where spending is restricted to capital schemes, to support cashflow and investment income
42. The capital reserves held by each former authority of Cheshire East have been reviewed and in the main the reserves contain the funding for committed capital schemes.
43. Departments have reviewed the current capital programme with a view to rationalising schemes where possible, and removing any which do not meet the aims and objectives of Cheshire East. Funding held in capital reserves can then be released to fund new capital schemes.
44. In considering the available funding for the capital programme, schemes will be cross referenced to Section 106 agreements and commuted sums and where possible funded from this source.

## **5. Conclusion**

- 45. Overall the Council is holding relatively high reserve balances due to the significant risks from creating a new authority and the current economic climate. This recognises local issues and allows the Borough Treasurer to comment favourably on the adequacy of reserves.
- 46. The establishment of protocols around the use of balances improves control and increases openness in financial reporting and management. This should reflect well in external assessment of the Council's financial standing.
- 47. The review of capital and earmarked reserves has been completed, and their rationalisation should simplify the presentation and understanding of the Council's reserves position. Reserves' positions will continue to be reviewed throughout the financial year.

# Background Papers

CIPFA, Local Authority Accounting Panel: Bulletin 55, Local Authority Reserves & Balances (2003)

General Fund Reserves ~ Risk Assessment Working Papers 2010

Final Accounts 2009/2010:

- Cheshire County Council
- Congleton Borough Council
- Crewe & Nantwich Borough Council
- Macclesfield Borough Council

Cheshire East Council Budget 2010/2011

# Annex A

## Protocol & Controls

### The Existing Legislative/Regulatory Framework

Sections 32 and 43 of the Local Government Finance Act 1992 require billing and precepting authorities in England and Wales to have regard to the level of reserves needed for meeting estimated future expenditure when calculating the budget requirement.

There are three significant safeguards in place that militate against local authorities over-committing themselves financially:

1. The balanced budget requirement
2. Chief Finance Officers' S114 powers
3. The External Auditor's responsibility to review and report on financial standing.

The balanced budget requirement is reinforced by section 114 of the Local Government Finance Act 1988 which requires the Chief Finance Officer to report to all the Authority's councillors if there is or is likely to be unlawful expenditure or an unbalanced budget. This would include situations where reserves have become seriously depleted and it is forecast that the Authority will not have the resources to meet its expenditure in a particular financial year. The issue of a section 114 notice cannot be taken lightly and has serious operational implications. The Authority's full Council must meet within 21 days to consider the S114 notice and during that period the Authority is prohibited from entering into new agreements involving the incurring of expenditure.

While it is primarily the responsibility of the local authority and its Chief Finance Officer to maintain a sound financial position, External Auditors have a responsibility to review the arrangements in place to ensure that financial standing is soundly based. In the course of their duties External Auditors review and report on the level of reserves taking into account their local knowledge of the Authority's financial 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 authorities or authorities in general.

### The Role of the Chief Finance Officer

It is the responsibility of the Chief Finance Officer to advise local authorities about the level of reserves that they should hold and to ensure that there are clear protocols for their establishment and use. There is no statutory minimum.

Local authorities, on the advice of their Chief Finance Officers, are required to make their own judgements on the level of reserves taking into account all the relevant local circumstances. Such circumstances vary. A well-managed authority, for example, with a prudent approach to budgeting should be able to operate with a relatively low level of general reserves. There is a broad range within which authorities might reasonably operate depending on their particular circumstances.

## **Good Governance**

It is important that Members take responsibility for ensuring the adequacy of reserves and provisions when they set the budget. CIPFA recommend that the respective roles of officers and Councillors in relation to reserves should be codified locally and given due recognition in the Constitutions. This codification should:

- state which council bodies are empowered to establish reserves
- set out the responsibilities of the Chief Finance Officer and Councillor – or group of Councillors – responsible for finance
- specify the reporting arrangements

## **A New Reporting Framework**

The Chief Finance Officer 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.

The level and utilisation of reserves will be determined formally by the Council, informed by the advice and judgement of the Chief Finance Officer. To enable the Council to reach its decision, the Chief Finance Officer should report the factors that influenced his or her judgement and ensure that the advice given is recorded formally. Where the advice is not accepted this should be recorded formally in the minutes of the Council meeting.

### **CIPFA recommended that:**

The budget report to the Council should include a statement showing the estimated opening general reserve fund balance for the year ahead, the addition to/withdrawal from balances, and the estimated end of year balance. Reference should be made as to the extent to which such reserves are to be used to finance recurrent expenditure this should be accompanied by a statement from the Chief Finance Officer on the adequacy of the general reserves and provisions in respect of the forthcoming financial year and the Authority's medium term financial strategy.

A statement reporting on the annual review of earmarked reserves should also be made at the same time to the Council. The review itself should be undertaken as part of the budget preparation process. The statement should list the various earmarked reserves, the purposes for which they are held and provide advice on the appropriate levels. It should also show the estimated opening balances for the year, planned additions/withdrawals and the estimated closing balances.