



RESERVES STRATEGY 2018/19 (Revised June 2018)

Introduction

1. The Reserves Strategy has previously been published, annually, as part of the Police and Crime Commissioner's (PCC's) annual budget setting report. It sets out the latest position and the strategy regarding the use of reserves in future years.
2. It is a statutory requirement that the Chief Finance and Commissioning Officer (CFO) presents a report to the PCC, as part of the budget approval process, which assesses the adequacy of reserves in the context of corporate and financial risks facing the PCC and the Chief Constable for South Yorkshire Police (SYP).
3. As part of the Police Funding Settlement for 2018/19, the Minister for Policing, Fire and Criminal Justice and Victims called for greater transparency in how public money is used locally. This included guidance as to the information PCCs should publish in relation to reserves.
4. This revised strategy provides information on the estimated level of reserves, both general and earmarked, balances currently held and explains how some of these will be applied over the medium term to help support the revenue budget and capital programme.

Background

5. Reserves may be used by the PCC for the annual budget and, over the longer term, as part of the overall Medium Term Resourcing Strategy (MTRS). There are a number of legislative safeguards in place that help prevent the PCC from over-committing financially. These include:
 - The requirement to set a balanced budget,
 - The requirement for PCCs to make arrangements for the proper administration of their financial affairs and the appointment of a CFO (Section 151 Officer) to take responsibility for the administration of those affairs,
 - The CFO's duty to report on the robustness of estimates and the adequacy of reserves,
 - The requirements of the Prudential Code, Treasury Management in Public Services Code of Practice and the Financial Management Code of Practice.

6. This is reinforced by Section 25 of the Local Government Act 2003, as amended by the Police Reform and Social Responsibility Act 2011, which requires the CFO to report on the robustness of estimates used for the budget and the adequacy of reserves and to report to the PCC, Police and Crime Panel and the External Auditor if there is, or is likely to be, unlawful expenditure or an unbalanced budget. This would include situations where the PCC does not have sufficient resources to meet expenditure in a particular year or where reserves have become depleted.
7. There is no statutory guidance on the 'right' level of reserves. Guidance from CIPFA confirms that PCCs should, on the advice of the CFOs, make their own judgements on such matters, taking into account relevant local circumstances and an assessment of risk. In a House of Lords debate of the policing precept in January 2018, the Minister of State stated that '5% of the revenue budget is deemed a reasonable level of reserves'.
8. There is also a requirement for three-year revenue forecasts across the public sector. This is achieved through the MTRS. Within the Comprehensive Spending Review, the PCC receives confirmation of revenue and capital grants from government for one year. This provides limited ability to focus on the levels of reserves and application of balances and reserves in the future medium term.
9. CIPFA's Prudential Code requires a CFO to have full regard to affordability when making recommendations about a PCC's future capital programme. Considerations include the level of long-term revenue commitments. When considering affordability, the PCC is required to consider all of the resources available and estimated for the future, together with the totality of their capital plans and revenue forecasts for the forthcoming year and future years as set out in the MTRS.
10. The PCC must retain adequate reserves so that unexpected demand-led pressures on budgets can be met without adverse impact on the achievement of the outcomes set out in the Police and Crime Plan. This will include known areas where financial implications are uncertain and more widely in respect of risks associated with assumptions of external support and income from Council Tax increases.

Types of Reserves

11. The PCC holds reserves which fall into two distinct categories:
 - **General Reserves:** these are necessary to fund any day to day cash flow requirements and also to provide a contingency in the event of any unexpected events or emergencies,
 - **Earmarked Reserves:** these have been created as a means of building up funds for specific purposes and involve funds being set aside to meet known or predicted future liabilities. By establishing such reserves, it will avoid liabilities being met from Council Tax or grant in the year that payments are made and impacting the revenue budget. A capital reserve is currently held to support future transformation of both the estate and use of technology to enable a more efficient future operating model.

Reserves Strategy

12. The required level of reserves needs to be assessed against potential risks that the PCC and the Chief Constable face in 2018/19 and beyond. The Finance Settlement from Government in 2018/19 offered all PCCs some certainty regarding the level of Council Tax policing precept which could be levied in 2019/20, but was contingent on progress against a number of efficiency milestones that have yet to be agreed by the Home Office.
13. The factors that need to be considered will include the financial risks associated with:
 - The deliverability of savings plans proposed to balance the revenue budget,
 - The potential for additional demand led pressures and costs e.g. the impact of fracking,
 - The likelihood of any additional government funding to offset unforeseen or unbudgeted expenditure, and
 - The nature of any historic events and potential liabilities arising from these events e.g. the legacy issues associated with the Hillsborough Disaster and cases of child sexual exploitation (CSE).
14. It has been previously established by the CFO that General Reserves, where possible, will be maintained at a level of approximately 5% of the total net revenue budget. Other earmarked revenue reserves or the capital reserve will be released to protect the level of General Reserves as far as possible. The impact of this on capital investment and the ability to fund potential future risks, such as policing fracking protests, will need to be assessed.

Reserves Balances 2018/19

15. At 1 April 2018 the total General and Earmarked Reserves were £46.5m. Of this, General Reserves (£13.4m) are broadly 5% of the net revenue budget. The remaining reserves are all earmarked, £25.6m for revenue and £7.5m for capital.
16. In order to balance the original 2018/19 budget, contributions from reserves of £7.3m were required. This involved releasing into the General Reserve:
 - £7.1m from the earmarked legacy reserve to fund expected legacy costs, based on the maximum Special Grant funding under the current rules from the Government, and
 - £2m from the earmarked innovation reserve to fund SYP's non-recurrent costs for transitioning to the new Target Operating Model, which is underpinned by three major reviews: Local Policing Review, Crime Review and Atlas Court Review.

This resulted in a slight increase in the General Reserves, after balancing the budget.

Future Reserves Balances

17. There is, however, significant risk and uncertainty that could affect the level and adequacy of reserves in future, without further efficiencies and savings generated by SYP beyond those assumed in the MTRS to support future budgets in the medium term.

18. Between 2018 and 2022 total reserves are expected to fall by £31m to £15.6m; with the General Reserve depleted to £4.1m (1.6%) at 31st March 2022. (See Appendix A). This assumes all Earmarked Reserves and the capital reserve are utilised to minimise the impact of Legacy costs under current Home Office Special Grant rules. Without this course of action, General Reserves would become overdrawn in 2021/22. To mitigate this, further savings would be required from the Chief Constable's budget. Appendix B shows the movement of reserves for South Yorkshire since 2012.

Impact of Legacy Costs

19. The level of legacy Costs, and uncertainty regarding central government funding support, are a significant risk to maintaining adequate levels of reserves in the future. The Legacy costs can be summarised as:
- Operation Stovewood: This is the work being undertaken by the National Crime Agency (NCA), with support from SYP, to investigate historic allegations of child sexual exploitation in Rotherham. In the previous two years, 85% of these costs have been met by the Home Office through Special Grant funding. These costs are expected to increase and continue to 2022/23 and at this time the level of Home Office support through Special Grant funding is unconfirmed. Allowing for anticipated Home Office Special Grant under the current rules, the estimated net funding gap which South Yorkshire will have to resource was reflected in the original budget and MTRS at February 2018.
 - Civil Claims: To assist budget setting, SYP's Legal Services team provided forecasts for 2018/19 and future years regarding Hillsborough and historic CSE-related civil claims. Allowing for anticipated Home Office Special Grant under the current rules, the estimated net funding gap which South Yorkshire will have to resource was reflected in the original budget and MTRS at February 2018.
20. In May 2018, the expected costs of legacy issues in 2018/19 and future years were updated. Due to the complexity of the issues, these costs can shift to later years depending on the pace of the Operation Stovewood investigations, or the progress of civil claims passing through the legal process. Future costs have now been projected over the next two years for CSE Civil Claims and the next five years for Hillsborough Civil Claims. As a result, the estimated contribution from reserves required in 2018/19 has reduced to £5.4m (as the costs are expected to be incurred in later years). This is reflected in Appendix A, which shows the updated movement of reserves over the MTRS period to 2021/22.
21. Although there is ongoing dialogue with the Policing and Fire Minister, there is a significant risk associated with legacy issues and the outcome of any Special Grant funding applications to the Home Office. Access to Special Grant funding is not guaranteed. Any unsuccessful application for special funding could affect the level and adequacy of reserves. Therefore the overall level will be kept under review during 2018/19 as part of medium term planning and the monitoring of risks.

Summary and Conclusion

22. Unlike General Reserves, Earmarked Reserves have been identified for specific areas of expenditure where there are anticipated costs that can only be estimated. It is therefore prudent for the PCC to identify such areas and set aside amounts that limit future risk. Appendix A, as previously stated, shows the movement of the Earmarked Reserves over the medium term and Appendix C details each of the Earmarked Reserves that exist as at 1 April 2018, by the prescribed Home Office categories.
23. Appendix A presents a future forecast of reserves based on the 2018/19 MTRS, approved in February 2018 updated for the latest forecast of legacy costs. The strategy has assumed that in order to retain General Reserves at 5%, or in positive balance, all Earmarked Reserves and the capital reserve will be released to support the General Reserves.
24. This will have an opportunity cost associated with it, in terms of constraining investment in transformation to the estate or in technology that would support the successful operation of a more efficient Target Operating Model. Additionally, to restore the General Reserves to 5%, savings from the revenue policing budget would be required, potentially impacting on the policing service in South Yorkshire. Hence dialogue remains open with the Home Office regarding certainty of government funding to support legacy costs.
25. This strategy will be reviewed annually with the PCC. During the year changes may occur in the MTRS, which may affect this strategy. Such changes will be monitored by the CFO and reported to the PCC appropriately.

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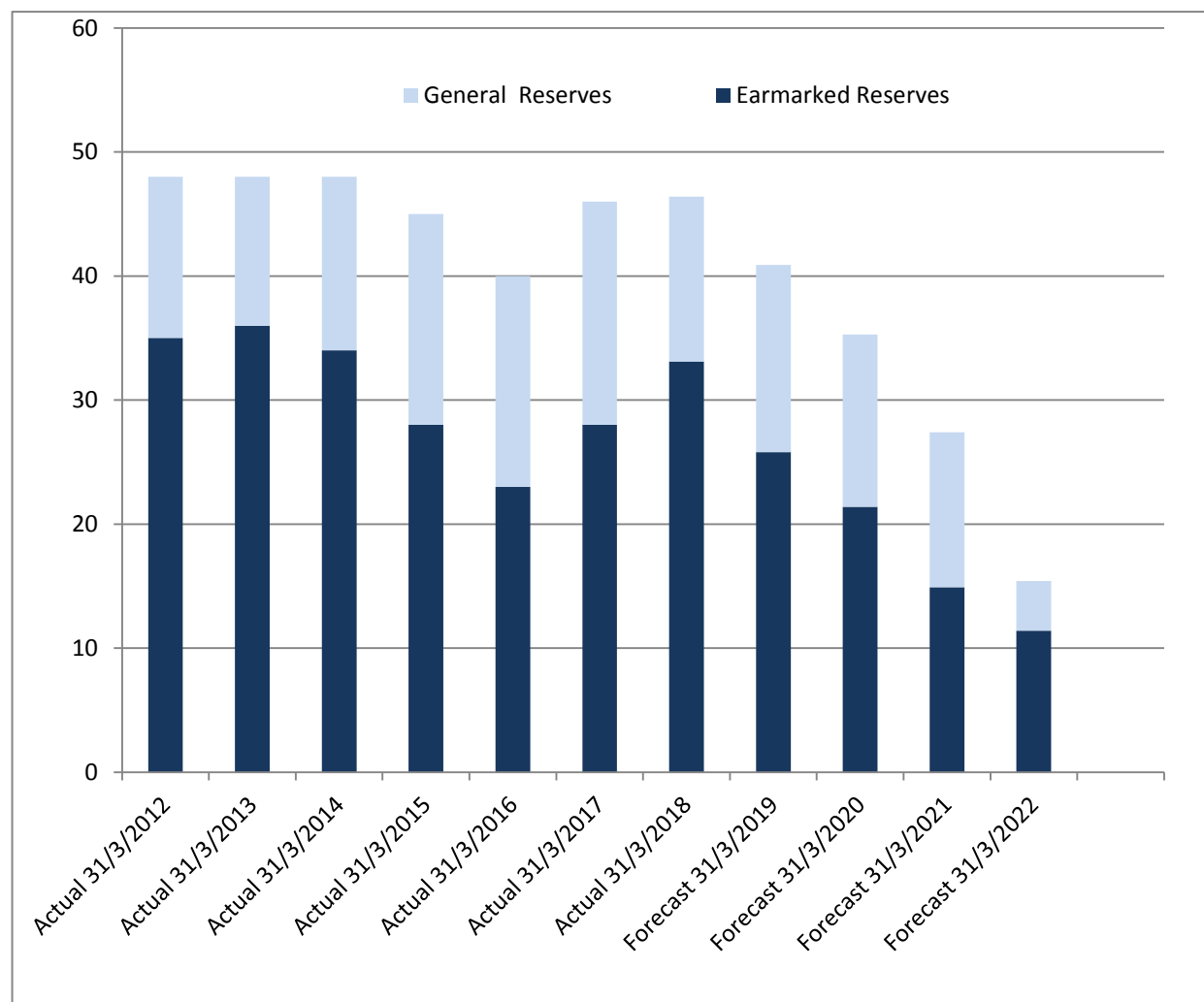
Reserves Forecast 2018 -2022

	Balance at 31/3/18	Budgeted movement	Forecast balance 31/03/2019	Forecast movement	Forecast balance 31/03/2020	Forecast movement	Forecast balance 31/03/2021	Forecast movement	Forecast balance 31/03/2022
General Reserves	13,389	1,785	15,174	-1,197	13,977	-1,390	12,587	-8,454	4,133
Rev Grant	3	0	3	0	3	0	3	0	3
PCC Commissioning	847	0	847	0	847	-847	0	0	0
PCC Innovation	2,000	-2,000	0	0	0	0	0	0	0
Insurance	11,422	0	11,422	0	11,422	0	11,422	0	11,422
Legacy Reserve	9,714	-5,213	4,501	-4,501	0	0	0	0	0
Redundancy Reserve	12	0	12	0	12	0	12	0	12
Devolved Budget	1,601	0	1,601	0	1,601	-1,601	0	0	0
Total Earmarked Reserves	25,599	-7,213	18,386	-4,501	13,885	-2,448	11,437	0	11,437
Capital Reserves	7,484	0	7,484	0	7,484	-3,955	3,529	-3,529	0
Total	46,472		41,044		35,346		27,553		15,570

Note:

- Based on the published MTRS, February 2018 and the latest (May 2018) profile of legacy costs and Special Grant under existing Home Office rules.
- Discussions are taking place with the Home Office and the Police and Fire Minister regarding the affordability impact for South Yorkshire of the current Special Grant rules.
- All Earmarked Reserves and the capital reserve are assumed to be utilised to minimise the impact of Legacy costs. Even so, General Reserves would fall to £4.1m (1.6%) in 2021/22 and become overdrawn in 2022/23. Without this course of action, General Reserves would be overdrawn in 2021/22. To mitigate this, further savings would be required from the Chief Constable's budget. The impact on capital investment and ability to provide for future risks, e.g. policing fracking protests, will need to be assessed.

Movement of Reserves – 2012-2022



Earmarked Reserves as at 1 April 2018

Home Office Category	Earmarked Reserve	Description/Use
Funding for planned expenditure over the period of the current medium term financial planning (£14.165m)	Revenue Grant Reserve (£0.003m)	This reserve is for any grant that has not been used to fund related expenditure to be used when it is incurred in future years.
	PCC Commissioning Reserve (£0.847m)	This reserve is for any underspends on the PCC's Commissioning Budget. It will be carried forward to use in future years for both revenue and capital spend.
	PCC Innovation Reserve (£2.0m)	This reserve was set aside to fund innovation initiatives and investments in schemes that will improve efficiency and reduce operating costs. This reserve will be used in 2018/19 to support SYP's transitional move to the new target operating model.
	Legacy Reserve	This reserve has been set aside from underspends on legacy costs to fund future

	(£9.714m)	potential liabilities in relation to Hillsborough and CSE.
	Devolved Reserve (£1.601m)	As part of the devolved financial management arrangements, budget holders are allowed to carry forward underspends up to approved limits to fund expenditure in future years.
Funding for specific expenditure beyond the current planning period (£7.484m)	Capital Reserve (£7.484m)	This represents the remaining amount set aside to support the PCC's capital investment programme.
As a general contingency/resource to meet other expenditure needs held in accordance with sound principles of good financial management (£11.434m)	Insurance Reserve (£11.422m)	This represents sums set aside to fund potential liabilities under the current insurance arrangements.
	Redundancy Reserve £0.012m)	This reserve is set aside to cover any future redundancy liabilities in relation to the Local Criminal Justice Board's (LCJB) Business Manager. The LCJB is funded by the PCC and external partners.