



NOTTINGHAMSHIRE
Fire & Rescue Service
Creating Safer Communities

Nottinghamshire and City of Nottingham
Fire and Rescue Authority

REVIEW OF RESERVES AND WORKING BALANCES

Report of the Chief Fire Officer

Date: 24 February 2017

Purpose of Report:

To seek the approval of the Nottinghamshire and City of Nottingham Fire and Rescue Authority to the minimum level of working balances sufficient to meet the needs of the Authority during the 2017/18 financial year and beyond.

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1. BACKGROUND

- 1.1 The Fire and Rescue Authority holds a level of working balances to meet specific risks and potential liabilities of a strategic, operational and financial nature.
- 1.2 The Chartered Institute of Public Finance and Accountancy (CIPFA) publishes guidance on the matter of financial reserves and sets out a number of specific risk areas that financial officers need to consider when setting the levels of balances.
- 1.3 As in previous years, a risk based approach has been taken to determine a reasonable level of balances. In accordance with this risk based approach, the level of balances required for 2017/2018 is £4,434,848. The main reasons for the change since 2016/2017 are explained in paragraphs 2.13 and 2.14.

2. REPORT

GENERAL RESERVES

- 2.1 The requirement for financial reserves is acknowledged in statute. 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.
- 2.2 There are also a range of safeguards in place that help to prevent local authorities over-committing themselves financially. These include:
 - i) The balanced budget requirement (sections 31a and 42a of the Local Government Finance Act 1992).
 - ii) The Treasurers' duty to report on the robustness of estimates and adequacy of reserves (under section 25 of the Local Government Act 2003) when the authority is considering its budget requirement.
 - iii) The legislative requirement for each local authority to make arrangements for the proper administration of their financial affairs and that the chief finance officer / proper officer has responsibility for the administration of those affairs (section 151 of the Local Government Act 1972).
 - iv) The requirements of the Prudential Code.
 - v) External auditors will confirm that there are no material uncertainties about an Authority's ability to continue operating, given its financial position.

- 2.3 Whilst it is primarily the responsibility of the local authority and its chief financial officer to maintain a sound financial position, external auditors will, as part of their wider responsibilities, consider whether audited bodies have established adequate arrangements to ensure that their financial position is soundly based. However, it is not the responsibility of auditors to prescribe the optimum or minimum level of reserves for individual authorities or authorities in general.
- 2.4 CIPFA does not prescribe a formula for calculating a minimum level of reserves. Local authorities, on the advice of their chief financial officers, should make their own judgements on such matters 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 level of general reserves appropriate for the risks (both internal and external) to which it is exposed. In assessing the appropriate level of reserves, a well-managed authority will ensure that the reserves are not only adequate but are also necessary. There is a broad range within which authorities might reasonably operate depending on their particular circumstances.
- 2.5 CIPFA sets out that reserves can be held for three main purposes:
- 2.5.1 A working balance to help cushion the impact of uneven cash flows and avoid unnecessary temporary borrowing – this forms part of general reserves;
 - 2.5.2 A contingency to cushion the impact of unexpected events or emergencies - this also forms part of general reserves;
 - 2.5.3 A means of building up funds, often referred to as earmarked reserves, to meet known or predicted requirements; earmarked reserves are accounted for separately but legally remain part of the General Fund.
- 2.6 The annual review of the risk assessment applicable to reserves and balances has recently been carried out by the Authority's Risk Manager and Head of Finance and the result of this risk assessment is given at Appendix A. This enables Members to see the key risks to which the Service is exposed and their estimated possible financial impacts.
- 2.7 There are three main categories of risk shown in the assessment: the risk of legal action being taken against the Authority, resulting in a financial loss; the risk of financial loss arising specifically from financial activities, and operational risks which could lead to financial loss. Where risks have been identified, control measures are in place to minimise either the likelihood or the impact of the risk and these are also shown in Appendix A.
- 2.8 The approach has examined each of the risk exposures and considered both the possible financial impact on the Service and the likelihood of occurrence. A risk factor has been allocated to each risk reflecting the likely frequency of occurrence of the risk based on historic experience and professional judgment. It should be noted that the underlying assumption is that not all of

these risk events will occur simultaneously and, to reflect this, the potential value of each financial impact is multiplied by its risk factor.

- 2.9 The approach also considers the extent to which financial risks can be transferred by way of insurances, thus creating a balance between insured and self-financed risk. Where insurances are in place, the risk value reflects the level of deductible within the insurance policy.
- 2.10 Residual risk is the extent to which the Authority remains exposed to risks which are neither insured nor provided for within revenue budgets or balances. The level of acceptable residual risk equates to the “risk appetite” of the Service and the estimated minimum level of balances reflects this risk appetite. The approach to the construction of the revenue budget for 2017/2018 has been to move away from traditionally low risk assumptions towards budgetary estimates which are more likely to reflect a realistic position rather than a cautious one and this change has made an impact on the latest estimate for the minimum level of balances.
- 2.11 The risk assessment review identified some changes in risks, mainly in terms of the increase (or sometimes decrease) in the potential costs of existing risks. The frequency of risk occurrence has also been reviewed in the light of another year of experience.
- 2.12 The updated risk assessment shows that an appropriate level of general reserves and working balances is £4.4m. This risk value has increased since last year by £590k and the main reason for this is that two new risks have been added and the reserve value in respect of two existing risks has changed significantly.
- 2.13 The two new risks are:
 - 2.13.1 The risk of overspending budgets due to the elimination of contingency budgets and budget assumptions based on a greater risk appetite. The risk value is estimated at 1% of the 2017/2018 revenue budget and equates to £407k. The risk factor is assessed as 0.5.
 - 2.13.2 The risk of unforeseen price increases due to currency exchange fluctuation. This risk was highlighted in a report to the Finance and Resources Committee in October 2016 and is assessed at £600k, although it is very difficult to quantify this risk. The risk factor is assessed as 0.5.
- 2.14 The two risks which have significantly changed are:
 - 2.14.1 The risk of unbudgeted redundancy costs due to current and on-going financial constraints, if savings cannot be found from elsewhere. The risk value remains as £500k but the risk factor has been increased from 0.5 to 1.0. This reflects the fact that the medium term budget is not yet balanced, as well as the uncertainties around the implications of the duty to collaborate with other emergency services when this becomes law.

2.14.2 The risk of higher than expected pay awards is assessed as 1% of the total pay budget and this risk value has been reduced from £494k to £309k to recognise the reduction in pay budgets in recent years. Although this risk appears to overlap with the risk of overspending budgets in paragraph 2.13.1 it remains a separate risk as it is concerned solely with the assumption made about pay inflation rather than any other budgetary assumptions. The risk factor remains as 1.0.

2.15 There are a number of other risks where minor amendments have been made to reflect changes in either risk value or in expected likelihood or impact in the light of another year's experience. The full risk assessment is given at Appendix A.

2.16 As set out in paragraph 2.4, the risk assessment which determines what the minimum level of reserves should be is carried out using the professional judgement of the Officers involved in the process. As well as the Risk Manager and the Head of Finance, the process involves consulting other Managers with particular areas of expertise in order to determine any new risks and to identify appropriate levels of risk value and risk frequency. This detailed review of risks inevitably results in fluctuations in the resulting minimum level and a review of the results of this process in previous years shows that, prior to this year, the highest minimum level was for the year 2014/15 (£4.2m), and that the lowest minimum level assessed was for 2013/14 (£3.4m). Over the past five years the risk-assessed minimum level of reserves has been: 2012/13 £3.5m; 2013/14 £3.4m, 2014/15 £4.2m, 2015/16 £4.0m and 2016/17 £3.8m. The Finance and Resources Committee regularly receives risk management reports, which show that corporate risks are regularly reviewed by Officers and that controls are in place to manage those risks. Even so paragraphs 2.13 and 2.14 above demonstrate that risk values can and do change, and the strategic risk register includes external risks which could impact on the Authority in the future.

The projected level of balances by 31 March 2017 is of the order of £7.5m which is higher than the £4.4m required, the excess being in the region of £3.1m. The budget report (elsewhere on this agenda) shows that significant pressure remains to achieve budget reductions over the next three years and that a contribution from reserves is required to balance the budget in 2017/2018. It is considered that it would be prudent to retain this excess sum within reserves to allow, if necessary, for a contribution from reserves to support the budget in 2017/2018, and potentially in the years following, whilst longer term budget savings are in the process of implementation.

It is appropriate to assure Members in this report that the level of balances to be held by the Authority will be sufficient to cover the risk based liabilities which may arise and the Treasurer will report on this as part of his duties under Section 25 of the Local Government Act 2003.

EARMARKED RESERVES

2.17 In addition to general reserves the Authority holds a number of earmarked reserves which are funds put aside to meet future items of expenditure. They may also have arisen from grants or donations which have been received in

anticipation of activities to be undertaken at a future date and therefore held on the balance sheet as earmarked reserves.

- 2.18 A full review of earmarked reserves was undertaken at the end of the last financial year. As part of the Authority's final accounts closedown process, all earmarked reserves will once again be reviewed by budget managers and Finance staff and the final earmarked reserves will be reported to Members within the Authority's Statement of Accounts 2016/2017.
- 2.19 The total value of earmarked reserves at 31 March 2016 was £3.501m. During the period up to the end of January 2017 there has been no requirement to use these reserves due to a revenue budget underspend, but a further contribution of £220k to top up the Organisation Transition earmarked reserve will be recommended to the Finance and Resources Committee in March 2017. If approved, this results in an expected earmarked reserves balance of £3.731m by 31 March 2017. Earmarked reserves and their forecast balances as at 31 March 2017 are shown in Appendix B.

3. FINANCIAL IMPLICATIONS

- 3.1 The maintenance of adequate working balances is a legal requirement under S27 Local Government Act 2003, and the Authority's Treasurer is charged with determining the adequacy of those balances or, as they are described in the Act, the "Controlled Reserve".
- 3.2 The risk assessment demonstrates that the level of balances should be in the order of £4.4m.

4. HUMAN RESOURCES AND LEARNING AND DEVELOPMENT IMPLICATIONS

There are no implications for human resources or learning and development arising from this report.

5. EQUALITIES IMPLICATIONS

An equality impact assessment has not been undertaken because this report relates entirely to accounting matters.

6. CRIME AND DISORDER IMPLICATIONS

There are crime and disorder implications arising from this report.

7. LEGAL IMPLICATIONS

The legal implications and requirements are set out in full within the report.

8. RISK MANAGEMENT IMPLICATIONS

The risk management implications are set out in full in the report and in Appendix A.

9. RECOMMENDATIONS

It is recommended that Members:

- 9.1 Note the results of the review of risks shown at Appendix A.
- 9.2 Approve the proposed minimum level of working balances of £4.4m for 2017/2018.

10. BACKGROUND PAPERS FOR INSPECTION (OTHER THAN PUBLISHED DOCUMENTS)

None.

John Buckley
CHIEF FIRE OFFICER

General and Working Balances Risk Assessment

APPENDIX A

Risk Description	Risk Effect	Control Measures	Insurable	Risk Value	Risk Factor Reflecting Frequency	Reserve Required	Revenue Budget
Discrimination cases	Reputational damage; Legal costs, employment tribunal costs unbudgeted	Professional HR advice, policies, procedures, management training, legal advice	N	500,000	0.25	125,000	0
Unfair Dismissal cases	Reputational damage; Legal costs, employment tribunal costs unbudgeted	Professional HR advice, policies, procedures, management training, legal advice	N	16,000	0.2	3,200	0
Settlement Agreements / Termination settlements	Reputational damage; Legal costs, employment tribunal costs unbudgeted	Professional HR advice, policies, procedures, management training, legal advice	N	100,000	1	100,000	0
Case for damages brought against the Authority	Reputational damage; Legal costs, Damages unbudgeted	Policies, procedures, management training, legal advice, procurement advice		1,000,000	0.2	200,000	0
Appoint independent investigator at request of elected Members	Cost of paying investigators	Policies, procedures, management training, legal advice, procurement advice	N	30,000	0.25	7,500	0
Discretionary Compensation scheme		Professional HR advice, policies, procedures, management training, legal advice	N	60,000	1	60,000	0
Equal pay claims	Reputational damage; Legal costs, employment tribunal costs unbudgeted	Professional HR advice, policies, procedures, management training, legal advice, equal pay audit	N	70,000	0.1	7,000	0
Injury Compensation Scheme awards above level budgeted for	Additional costs	Policies and procedures, training etc to reduce likelihood of injury. Occupational Health devising new interventions to reduce risk.	N	7,000	1	7,000	0

Risk Description	Risk Effect	Control Measures	Insurable	Risk Value	Risk Factor Reflecting Frequency	Reserve Required	Revenue Budget
Ill health retirements higher than number budgeted for	Additional costs	Professional HR advice, policies, procedures, management training, legal advice, (no earmarked reserve left)	N	135,000	2	270,000	0
Pension Ombudsman Rulings	Compensation award payment	Pension administration expertise bought in	N	5,000	1	5,000	0
Medical Appeals re FFPS	Cost of appeal process	IQMP policy and advice taken	N	8,000	1.5	12,000	0
Local/national industrial dispute	Potential loss of service; risk of non-compliance with statutory duties and ensuing legal case / fines; selective industrial action may not result in sufficient underspend to cover additional costs. Potential ministerial intervention and ensuing reputational damage.	Maintain adequate contingency cover. Contingency arrangements well tested during 2013-2015 industrial action.	N	495,000	1	495,000	0
Non-compliance with environmental legislation - support for legal proceedings	Cost of responding to enforcement action	Acquisition of permits / licences; planned drainage works; site risk profiles	N	70,000	0.25	17,500	0
Negligent fire safety work	Litigation	Training, procedures, effective SLA's with an appropriate allocation of liabilities	Y	10,000	0.1	1,000	0
Increase in numbers of vulnerable people due to economic climate	Loss of council tax precept income, additional cost of fire prevention activity	No controls in place	N	204,000	0.5	102,000	0
Change in legislation / regulations	Loss of use; cost of modifications and replacements	Continuous review process	N	100,000	0.1	10,000	0
Unforeseen general change in legislation / Major Incident Reviews	Increased costs of working due to doing more or doing things differently & costs of training	Awareness	N	100,000	0.2	20,000	0

Risk Description	Risk Effect	Control Measures	Insurable	Risk Value	Risk Factor Reflecting Frequency	Reserve Required	Revenue Budget
Risk to health, safety & welfare of employees	Litigation; legal costs & staff absence	Operating procedures; training; written safety policy; risk assessments	Y	10,500	3	31,500	0
HSE Interventions	Cost of remedial measures; cost of fine; fees for HSE intervention, indirect costs of covering internal resources used to investigate the issue etc.	Operating procedures; training; written safety policy; risk assessments	N	315,000	0.1	31,500	0
Reignition or other negligence	Reputational, financial	Operating procedures	Y	10,500	1	10,500	0
Breach of security	Loss of confidential data; Information Commission fines	Protective security measures; ICT policies; physical, technical and people security measures; Information Governance Officer post; Data Protection policy	N	80,000	0.125	10,000	0
Redundancies due to current and on-going financial constraints, if savings cannot be found from elsewhere	One-off cost of redundancy payment and potential pension strain is too high a cost to budget for within the revenue budget	Business case and payback period	N	500,000	1	500,000	0
Discovery of major property structural problem that restricts / prevents use of all or part of building(s)	Loss of use; cost of repair; impairment to operational effectiveness	Continuity plans, repair and refurbishment programme	P	600,000	0.1	60,000	0
Fire, flood or other peril	Loss of use; cost of repair; impairment to operational effectiveness	Continuity plans, repair and refurbishment programme	Y	1000	0.2	200	0
Theft of assets	Disruption	Safety procedures	Y	1000	1	1,000	0
Own damage	Disruption	Risk management	Y	1000	1	1,000	0
Serious injury to public	Reputation, cost, staff time	Training and procedures	Y	10,500	0.1	1,050	0
Damage to vehicle	Loss of use; cost of repair; replacement vehicle hire; lease extensions	Road Risk Group - review of road risk; training; inclusion of vehicle safety options	Y	1,000	100	100,000	35,000

Risk Description	Risk Effect	Control Measures	Insurable	Risk Value	Risk Factor Reflecting Frequency	Reserve Required	Revenue Budget
Appliance written off in an accident	Loss of use; insurance receipt may not cover cost of replacement	Road Risk Group - review of road risk; training; inclusion of vehicle safety options	Y	120,000	0.5	60,000	0
Multiple appliances written off in major incident (maximum 2 appliances)	Loss of use; insurance receipt may not cover cost of replacement; appliance degradation enacted; impact on service delivery; impact on appliance replacement programme	Training and procedures; appliance degradation procedure	Y	200,000	0.1	20,000	0
Major vehicle defect (affecting part of fleet)	Loss of use; cost of rectifying defect if beyond warranty	Mutual assistance, robust and routine fleet inspections	N	150,000	0.2	30,000	0
Unforeseen increase in fuel prices	Increased costs	None	N	70,000	1	70,000	0
Increased risk of overspending budgets due to elimination of contingency budgets and budget assumptions based on greater risk appetite	Overspend against revenue budget in year which will have effect of reducing general reserves by the amount of the overspend	Focus on realistic assumptions, rather than risky assumptions. Close monitoring of budget throughout year to allow corrective action to be taken	N	407,240	0.5	203,620	0
Major operational equipment defect	Loss of use; cost of modifications and replacements	Inspection routines	N	100,000	0.2	20,000	0
Major fraud	Financial loss	Internal control	Y	5,000	0.1	500	0
Higher than expected pay awards	Large hit on pay contingency	Maintain adequate general contingency	N	309,000	1	309,000	0
Significant change in interest rates	Increased costs / loss of income	Prudential code and treasury management indicators	N	120,000	0.2	24,000	0
Unforeseen price increases due to currency exchange fluctuation	Increased costs / potential for reduced competition	May not be possible to avoid through contractual obligations	N	600,000	0.5	300,000	0
Unforeseen indirect impacts of changes to pension regulations	Potential additional NI costs, potential increased membership so employers' superannuation costs etc.	Monitor ongoing consultations etc and budget for likely impacts as soon as clear	N	140,000	0.5	70,000	0

Risk Description	Risk Effect	Control Measures	Insurable	Risk Value	Risk Factor Reflecting Frequency	Reserve Required	Revenue Budget
Business failure of bank or investment counterparty	Loss of working capital or investment funds up to £2m	Treasury management strategy, risk analysis of investment options and counterparties	N	2,000,000	0.2	400,000	0
Failure of counterparty to purchase fixed asset for sale	Loss of capital receipt to be used to finance capital programme, or contribute towards required savings – financial loss	Legal advice for major contracts and due diligence including risk analysis of prospective purchasers	N	2,500,000	0.167	417,500	0
Unanticipated loss of short term income i.e. from precept, non-domestic rates or government grant	Timings of budget process may not allow sufficient time to plan for such changes	Network of Chief Financial Officers keep abreast of developments.	N	420,750	0.5	210,375	0
Major CBRN / terrorist incident	Reduction in capability to respond	Multi-agency plans; New Dimensions equipment; BCM plans; Response degradation policy; Mutual Aid	N	81,448	0.1	8,145	0
Natural disasters	Reduction in capability to respond	Multi-agency plans; New Dimensions equipment; BCM plans; Response degradation policy; Mutual Aid	N	81,448	0.5	40,724	0
Multiple large incidents	Reduction in capability to respond	Multi-agency plans; New Dimensions equipment; BCM plans; Response degradation policy; Mutual Aid	N	81,448	0.3	24,434	0
Hot or dry summers	Increased retained call-outs	None	N	220,000	0.33	72,600	0
TOTALS				12,046,834		4,469,848	35,000

Minimum level of general reserves 2017/2018

£4,434,848

Earmarked Reserves

APPENDIX B

Reserve	Balance 31 March 2016 £	Estimated Spend Against Reserve in 2016/17 £	Estimated Contributions to Reserves in 2016/17 £	Estimated Balance 31 March 2017 £
FUNDED BY GRANTS				
LPSA Reward Grant	173,952			173,952
Fire Investigation	119,978			119,978
Safe as Houses - Smoke Alarms	21,661			21,661
Community Safety - Innovation Fund	200,594			200,594
Resilience Crewing and Training	451,740			451,740
Thoresby Estate Charitable Trust	3,011			3,011
Transparency Grant	7,679			7,679
Safe and Well	0		10,000	10,000
	978,615	0	10,000	988,615
CREATED FROM REVENUE				
Pensions Ill Health	309,322			309,322
On Fire Fund - Fire Safety	86,749			86,749
Fire Control Transition	143,123			143,123
Agresso Development	15,680			15,680
ICT Sharepoint Internet/Intranet	97,086			97,086
Operational Equipment	10,000			10,000
Capital Reserve	1,154,276			1,154,276
Organisation Transition - one off costs	148,513		220,000	368,513
Swan Project - Ashfield	217			217
Tri-Service Control Phase 2 Project	219,815			219,815
Fire Cadets Project	22,648			22,648
Backlog Buildings Maintenance	95,000			95,000
Taxation Compliance	10,000			10,000
Communications Development	200,000			200,000
IT Systems	9,662			9,662
	2,522,091	0	220,000	2,742,091
TOTAL	3,500,706	0	230,000	3,730,706