

APPENDIX 1

THE FINANCIAL RESERVES POLICY

1. Introduction

- 1.1 It is good financial practice that the Council has a documented and approved Financial Reserve Policy.
- 1.2 The Statutory Basis for Accounting for and Disclosing Reserves in Scottish Local Government Bodies (2021) provides mandatory guidance from LASAAC in respect of Local Authority Reserves and Balances.
- 1.3 The following Policy reflects the key messages from the guidance and also outlines the practical application for the Council.

Deleted: Local Authority Accounting Practice (LAAP) Bulletin 99 published in July 2014

Deleted: advice from CIPFA

Deleted: LAAP Bulletin

2. Types of Useable Reserves Operated by the Council

- 2.1 Useable reserves are those that can be applied to fund expenditure whereas Unusable Reserves are restricted to accounting entries.
- 2.2 General Fund Reserve
The General Fund Reserve is split into a non-Earmarked portion and Earmarked Reserve. The former is often referred to as the "Free Reserve" and it is held for unforeseen emergencies and contingencies. The current Council policy is that the Free Reserve should not be lower than £5 million which represented 2.5% of annual turnover where turnover is defined as General Government Revenue Grant Income and Council Tax Budgeted Income when the policy was approved. 2.5% of the current General Services Revenue Budget for 2021/22 is £5.5million.
- 2.2.1 Earmarked Reserves are sums of money retained for future use for a specific purpose or commitments made which cannot be accrued at year-end due to not being in receipt of the service or goods. In recent years a greater use has been made of ear-marked reserves than had previously been the case to ensure than any windfall funding is directed towards Council priorities, including the transformation of Council services.
- 2.2.2 The following ear-marked reserves are held within the General Fund Reserve:

Deleted: or

Deleted: 2018/19

Deleted: £5.04

Deleted: Within

Deleted: the most significant earmarked balance is for the Devolved School Management (DSM) scheme which facilitates balances being carried forward from year to year by individual schools.

Fund	Purpose of fund	Balance @31 March 2021 £000s
Covid-19 funding	Carry forward funds given as part of General Revenue Grant in 2020/21 to deal with issues arising from the pandemic	16,421

Fund	Purpose of fund	Balance @31 March 2021 £000s
Transformation of services	To facilitate the Improvement and Modernisation Programme (IMP)	3,664
Council priorities	To advance projects related to achieving Council priorities	2,881
Devolved School Management (DSM)	To enable DSM budgets to be managed over more than one financial year, per the DSM scheme	1,343
Pupil Equity Funding (PEF)	To enable PEF to be managed over the academic year, per the funding conditions	802
Expansion of Early Years and Childcare (ELC)	To carry forward specific grant funding to use for the purposes the grant was given	573
Other		839
Total		26,523

2.2.3 Funds which are not earmarked for specific purposes are set aside to deal with unexpected events or emergencies or at the discretion of Members.

2.3 Housing Revenue Account (HRA)

These are funds which are for use by the Council's Housing Service to smooth expenditure or to fund emergencies. The funds are ring-fenced for the Council's Housing Service.

2.4 Statutory Funds

There are also amounts set aside from the General Fund and HRA balances in Statutory Funds to provide for future expenditure. These are the Repairs and Renewals Fund, which ~~was established~~ to assist with uninsured losses to council properties arising from flooding incidents ~~but which can be used for any property maintenance or repairs~~, and the Insurance Fund, which ~~was~~ set aside to pay any uninsured losses regarding school buildings ~~but which can be used to meet any insurable costs elected by the Council to self-insure~~.

Deleted: is

Deleted:

Deleted: is

2.5 Capital Fund

The Capital Fund is used to directly finance future capital expenditure.

2.6 Capital Grants Unapplied

Holds grants and contributions received towards capital projects. The balance represents funds which have yet to be applied to meet expenditure and would otherwise require repayment.

2.7 Capital Receipts Reserve

Holds the proceeds from the disposal of land or other assets and its use can only be for capital purposes ~~as a general rule. However for a four year period ending 31 March 2021 Scottish Government gave a concession that capital receipts could be used to fund expenditure anticipated to give rise to recurring savings and the Council has taken advantage of this concession.~~

3. Governance of Reserves

3.1 The governance arrangements are as follows for each reserve:

3.1.1 General Fund Reserve

- Level of Free Reserves agreed as part of the Reserve Policy and reviewed no less frequently than 3 yearly by the ~~Policy and Resources Committee~~ ~~or full Council~~.
- Projected Balance reported to the Policy and Resources Committee when expenditure for the year is forecast.
- Reported annually to the full Council as part of the review of the Financial Strategy.

Commented [LP1]: Need to amend to Corporate Committee if approved

3.1.2 Earmarked Reserves

- Creation of Earmarked Reserves approved by ~~the Policy and Resources Committee~~ ~~or full Council~~.
- Update in respect of Earmarked Reserves reported monthly to the Corporate Management Team.

Commented [LP2]: As above

3.1.3 Repairs and Renewal Fund

- Additions to the Repairs and Renewal Fund require Policy and Resources Committee approval.

This fund was set up specifically to provide for expenditure arising from flooding incidents prior to the construction of flood alleviation schemes. As part of the financial planning process use of the General Services portion of the fund has been proposed for a number of years. This use has not been yet required but is still planned.

Formatted: Indent: Left: 2.54 cm, No bullets or numbering

Formatted: Normal, Indent: Left: 1 cm, Hanging: 0.25 cm, No bullets or numbering

Formatted: Font: (Default) Arial, 12 pt

3.1.4 Capital Receipts Reserve

- All receipts from sales of assets are paid into the Capital Receipts Fund unless otherwise approved by the Policy and Resources Committee.
- Capital Receipts Reserve update reported as part of the quarterly monitoring of the Capital Plan to Policy and Resources Committee.
- Decisions to utilise the Capital Receipts Fund approved by the Moray Council.

3.1.5 Insurance Fund

- Insurance Fund Balance reviewed and reported as part of the Annual Accounts to the Moray Council.

3.2 Earmarked Reserves Process

3.2.1 An earmarked reserve cannot be established without the approval of the Chief Financial Officer, and the Policy and Resources Committee or full Council.

Deleted: Head of Financial Services

3.2.2 For each earmarked reserve there needs to be a clear documented understanding of the purpose of the reserve, the timescale for which the reserve is required and anticipated phasing.

3.2.3 For earmarked reserves projecting over £50,000 of spend during the year then the annual spend requires monthly phasing.

3.2.4 As part of the year end accounts the remaining balance and continuing purpose of the earmarked reserve requires reviewing by the budget holder and approval by the Chief Financial Officer.

Deleted: e

3.2.5 Any earmarked reserve not required is to be written back to free General Fund reserves.

Deleted: the

4. Role of the Chief Financial Officer

Deleted: Head of Financial Services

4.1 The Chief Financial Officer is responsible for advising on the targeted optimum levels of reserves the Council aims to hold. The Council based on

Deleted: Head of Financial Services

that advice should then approve the appropriate reserve strategy as part of the financial planning process.

Deleted: budget

5. Reporting and Review

5.1 The Reserves Policy requires to be reviewed and approved no less frequently than three yearly and reported to the Policy and Resources Committee or full Council.

5.2 In the event that it is projected that the Council's Non-Earmarked General Fund Reserve ('Free General Reserve') will fall below the approved limit, then the Chief Financial Officer should report no later than to the next meeting of the Policy and Resources Committee explaining the reasons for this shortfall and the options available to rectify the situation.

Deleted: Head of Financial Services

6. Level of Free General Reserve

Deleted: s

6.1 The level of free general reserve held by the Council is a key component in risk management for the Council and so it is considered appropriate that in determining the minimum level of reserves to be held by the Council that explicit recognition of the risks likely to impact on that balance are recognised.

Deleted: s

6.2 An update to the Council's corporate risk register was approved by Education, Communities and Organisational Development Committee at its meeting on 26 May 2021 and includes the following risks with potential financial impact:

Deleted: Council

Deleted: 6 June 2018

1. Demand for services outstrips available budget
2. Savings required to be made to create a sustainable financial operating environment
3. MIJB – no council control but liability for around 40% overspend, (if any).
4. Inability to recruit
5. Impact of climate change and severe weather events
6. Regulatory penalties: Data protection breaches, Health and Safety incidents
7. Economic recovery – poor local economic performance could result in lost Council Tax and Non Domestic Rates income, lower rentals from the industrial estate and pressure on services

Deleted: Health and Safety incidents

The mitigations in place for these risks are set out in the risk register.

7.3 The following points of detail should be considered:

Service demand

Formatted: Indent: Left: 1.27 cm

6.3.1 There is anticipated to be increasing demand for council services arising from demographic growth. There is an element of the council's allocation of General Revenue Grant which is based on population numbers. This is

based on statistical projections of population numbers from the National Records of Scotland (NRS). Historically these projections have lagged behind the actual growth of Moray's population, which means that existing budgets are under pressure to accommodate population based service growth. A report to the Economic Growth, Housing and Environmental Sustainability Committee on 24 August 2021 highlighted some particular concerns with current population projections for Moray.

6.3.2 Savings

6.3.2 The Council requires to make significant savings and as yet there is no defined plan to meet the whole funding gap. There is an underlying overspend which had previously been funded from a combination of retention of Non Domestic rates income under the Business Rates Incentivisation Scheme (BRIS) and use of reserves. It is currently anticipated that there will be funding available in the covid ear-marked reserve to cover the underlying budget gap in 2022/23 and contribute towards it in 2023/24.

6.3.3 Savings arising from transformation programmes generally (i) take time and (ii) require upfront funding. A cushion of reserves will be needed for this process and as indicated above the uncommitted element of the covid ear marked reserve is currently planned to be used to plug the budget gap. Further reserves require to be identified for investment in change.

6.3.4 The Council has been making significant savings since 2008. As time progresses savings are more difficult to find and there is a risk that savings offered are more difficult to achieve. Savings which rely on increased income from charging for services are particularly at risk as the initial impact of increased charges is usually decreased uptake of service.

6.3.5 A combination of the impact of the UK leaving the EU and the effect of the pandemic is causing shortages of labour and goods, resulting in current high level of construction costs and above target general inflation as measured by CPIH is anticipated later in this financial year. This may have on-going impacts on costs which could result in further savings being required.

6.3.6 The pay award for 2021/22 has not been agreed for any of the employee groups. Higher inflation could play out in continuing increased pay demands. The Council is looking at consolidating the Living Wage into its pay scales. This will have cost implications. Various options are currently being considered.

MIJB

6.3.7 The MIJB budget is also in excess of agreed funding. Previously planned savings were put on hold during the response to the pandemic.

Deleted: The Council is seeing growth of demand for care placements for children and the value of a single case can be a significant unplanned pressure. This would appear to be a national trend.

Page Break

Formatted: Font: Bold

Deleted: 3

Deleted: – such funding will no longer be possible.

Deleted: 4

Deleted: is likely to

Deleted: As an illustration the Designing Better Services programme achieved savings of £3 million over an 8 year time frame. There were no savings in year 1.

Deleted: 5

Deleted: 6.3.6 Part of the council's suite of short term savings measures is the Make Do and Mend approach to asset management and capital spend. This approach carries with it an increased risk of major element failure. This is a particular risk regarding the school estate

Deleted: On top of this underlying overspend there is currently an overspend against budget. The Chief Officer is committed to providing a recovery plan that will secure a balanced budget position for 2019/20.

Deleted: 6.3.8 .

Deleted: The Council's insurers increased premiums in 2018/19 because of the level of employer's liability claims in recent years. Future risks regarding insurance claims arise from the reduction in roads maintenance budgets. The council has a good record in regard to claims for damage caused by pot-holes but may find it less easy to defend claims in the light of cuts in service. In addition, a saving proposal to increase the level of insurance excess may incur greater expenditure than forecast.

Recruitment

- 6.3.8 If the Council is unable to recruit into posts then these must be covered by other staff working additional hours, agency staff or out-sourcing. As a general rule, it is more expensive to employ agency staff or to outsource than to employ Council staff.

Climate Change and severe weather events

- 6.3.9 The Council has recognised a climate change emergency and adopted a Climate Change Strategy. This recognises that severe weather events are increasingly likely. In the past the Council has had to deal with damage to Council buildings, roads, bridges and harbour infrastructure due to severe weather events, as well as the costs of immediate response eg provision of alternative accommodation for people whose houses have been affected.
- 6.3.10 The Bellwin scheme, which is designed to assist councils in dealing with major emergencies, does not cover all expenditure incurred by a council and in particular assumes that the council will meet all costs up to the threshold (currently 0.2% of the council's net budget).
- 6.3.11 The winter maintenance budget is set for a mild winter. Unlike many other councils, Moray does not hold a specific ear-marked winter maintenance reserve for bad winters.
- 6.3.12 There are suggestions that energy prices may rise to fund developments in energy production such as green hydrogen.

Regulatory penalties

- 6.3.13 The General Data Protection Regulation (GDPR) has a regime of potentially swingeing penalties for breach of GDPR. Health and Safety breaches can incur fines and can result in higher insurance costs.

Economic Recovery

- 6.3.14 The risk of a prolonged economic downturn following the pandemic and Britain's withdrawal from the European Union is recognised in the Corporate Risk Register. An economic downturn would be likely to have both direct – in terms of lower Council Tax, Non Domestic Rates, housing and property rental and increased benefit claims – and indirect – in terms of changing and increasing demands on Council services – and is compounded by the continued restrictions on construction activity, supply chain shortages and high current level of construction inflation.
- 6.4 In addition to those risks specifically included in the Corporate Risk Register, the largest area of uncertainty of direct relevance to the Council's finances is the level of income available to Scottish Government – with more money generated directly or indirectly from a share of national taxes the income available for Holyrood to distribute is less certain than under the Block Grant system. The medium to long-term impact of both the pandemic

Formatted: Indent: First line: 0 cm

Formatted: Font: Not Bold

Formatted: Font: Bold

Deleted: In recent years there have been incidents of road subsidence, requiring repair at costs between £300,000 and £500,000; landslips at Portknockie, and harbour wall breaches at both Lossiemouth and Cullen harbour, again incurring significant cost to repair. This pattern of ongoing weather damage seems unlikely to abate, particularly given the reduction in expenditure on the council's road asset

Deleted: .

Formatted: Font: (Default) Arial, 12 pt

Formatted: Indent: Left: 1.27 cm, Space After: 10 pt, Line spacing: Multiple 1.15 li, No bullets or numbering

Deleted: introduction of the

Deleted: brought new and increased,

Deleted: into play

Formatted: Indent: Left: 1.27 cm, No bullets or numbering

Formatted: Font: Bold

Deleted: k

Formatted: Font: (Default) Arial, 12 pt

Formatted: Font: (Default) Arial, 12 pt

Formatted: Normal, Indent: Left: 0 cm, Hanging: 1.5 cm, No bullets or numbering

Deleted:

Formatted: Font: (Default) Arial, 12 pt

Deleted: it should be noted that as the council has reduced its levels of reserves over the last few years. It has also increased the exposure to risk which the council has from budget assumptions used in the financial planning process, as there is less leeway to manage unexpected calls arising from funding being less than expected or expenditure more. Increased demand has been recognised in the risk register, but risk arises also from pay awards and other inflation based increases.

Deleted:

Deleted: Potential unknowns are:¶

¶

Pay awards – the pay offer for 2018/19 is not agreed¶
The council pay award tends to have a (delayed) effect on pay for organisations delivering services to the council, particularly in the areas of care services, where the council and private or third sector employers are competing to recruit and retain from the same pool of people¶

The impact of Brexit on sterling and thence on (particularly) ICT contract prices¶

Energy prices, with suggestions that there may be significant price increase

Deleted: .¶

Deleted: <#>Inflation is running above the government's target rate. The council does not allow for general inflation but this may influence the likelihood of overspend in an increasingly constrained environment.¶

Formatted: Font: (Default) Arial, 12 pt

Deleted: I

and the UK withdrawal from the EU are unknowns both of which could have significant impact on revenue generated by Scottish Government

6.5 CIPFA in the draft suite of Financial Resilience Indicators (for use in England and Wales) include reference to the availability of council reserves as a test of resilience. In essence the lower the level of council reserves the less resilient that council is in regard to the ability to cope with unplanned events. Benchmarking against other Scottish local authorities prior to 2020/21 shows Moray to have a fairly typical minimum approved level, with 1.5% - 4% of annual turnover being roughly the range reported and 2% the most common. The position for all Scottish local authorities changed dramatically for the year ended 31 March 2021, with very significant increases in funding announced and received towards the end of that financial year, largely directly related to the pandemic, although mainly paid as redetermination to General Revenue Grant. Moray's share of this funding has been ear-marked, and a considerable proportion of the ear-marked funding is estimated to be required in 2021/22. The question of the appropriate policy position regarding free general reserve should be considered without reference to this ear-marked reserve.

Deleted: 6.5 Another factor of note is the extension of time for insurance claims for historic child abuse claims. Claims can now be made for any time after 1964 (previously restricted to 3 years).¶

Deleted: 6

Deleted: The table in para 6.7 below provides an assessment of financial risks that informs the council's 2.5% position.

6.7 As a test of the reasonableness of the policy position on free general reserve the following table gives some guidance:

Risk	Proposed measure	£000s
Rise in demand		
Pay award	Increase from <u>provision in 2021/22 budget to Scottish Government public sector pay policy</u>	700
	<u>Further increase to pay demand</u>	1,000
<u>Living Wage</u>	<u>To be determined following modelling</u>	
MIJB	Level of budget above funding (Council share)	726
	<u>Allowance for overspend / demographic growth (Council share)</u>	1,000
Insurance claims – employer's liability	Average claims over last four years (<u>not updated – claims have been lower but excess increased</u>)	250
Insurance claims – pot holes	Based on previous numbers of claims in a bad winter	100
Infrastructure failure	Average over last 2 years (<u>not updated</u>)	600
Emergency event	Bellwin threshold (<u>2020/21 – latest published figures</u>)	443
Winter maintenance	Average spend above budget for last two years	600
Budget variance	Based on average Directors of Finance PIs (<u>0.8% variance</u>) <u>for 2018/19 and 2019/20 as 2020/21 not a typical year because of pandemic</u>	1,700
Government grant less than forecast	Sensitivity 1%	1,680
Interest rates	Increase in loans pool rate from higher borrowing charges (<u>2020/21 rate plus 100 bps</u>)	865
<u>Increase in Council Tax Reduction</u>	<u>Level of increase during pandemic</u>	330
<u>Reduction in Council Tax collection rate</u>	<u>By 0.5%</u>	300
<u>Reduction in Industrial Estate rentals</u>	<u>By 5%</u>	100
Total		10,394

A free reserve of £5 million gives 48% coverage of the quantified risks above. It is unlikely that all of these scenarios would arise and so 48% coverage is considered reasonable. It is not considered prudent to reduce the level of free reserve below £5 million. This currently represents 2.33% of the Council's General Services revenue budget.

Deleted: that level

Deleted: Average growth in out of area placements for the last 2 years

Deleted: 600

Deleted: 500

Deleted: g

Deleted: target to current rate of inflation (2019/20 budget provision)

Deleted: 1,300

Deleted: 0

Deleted: 400

Deleted: 350

Deleted: of last 2 years

Deleted: 2,000

Deleted: 1

Deleted: 1,500

Deleted: 1,350

Deleted: 2015/16

Deleted: 9,950

Deleted: 50

Deleted: 50

Deleted: 2.47

