

<b>ISLE OF ANGLESEY COUNTY COUNCIL</b>	
<b>Report to</b>	<b>Executive Committee</b>
<b>Date</b>	<b>3 December 2012</b>
<b>Subject</b>	<b>Review of Financial Reserves and Balances</b>
<b>Portfolio Holder(s)</b>	<b>Councillor John Chorlton</b>
<b>Lead Officer(s)</b>	<b>Interim Head of Function (Resources)</b>
<b>Contact Officer</b>	<b>Gill Lewis (Ext. 2620)</b>
<b>Nature and reason for reporting</b>	
To consider the level of Financial Reserves and Balances and demands on them, and advise on the potential release of reserves.	

<b>A – Introduction / Background / Issues</b>		
<p>This report updates previous assessments of financial reserves. The purpose of the review is to ensure that the reserves are still required, adequate for the purpose intended and not excessive. We base the review on Cipfa's Bulletin on Local Authority Reserves and Balances. The financial reserves are reviewed on an ongoing basis but this formal review is conducted each year in advance of considering the budget.</p>		
<b>B – Considerations</b>		
See attached		
<b>C – Implications and Impacts</b>		
<b>1</b>	<b>Finance / Section 151</b>	Author of report
<b>2</b>	<b>Legal / Monitoring Officer</b>	
<b>3</b>	<b>Human Resources</b>	
<b>4</b>	<b>Property Services</b> (see notes – separate document)	
<b>5</b>	<b>Information and Communications Technology (ICT)</b>	
<b>6</b>	<b>Equality</b> (see notes – separate document)	
<b>7</b>	<b>Anti-poverty and Social</b> (see notes – separate document)	
<b>8</b>	<b>Communication</b> (see notes – separate document)	
<b>9</b>	<b>Consultation</b> (see notes – separate document)	
<b>10</b>	<b>Economic</b>	
<b>11</b>	<b>Environmental</b> (see notes – separate document)	
<b>12</b>	<b>Crime and Disorder</b> (see notes – separate document)	
<b>13</b>	<b>Outcome Agreements</b>	

<b>CH – Summary</b>
<p>To assist in budget planning, I can advise the Executive that they may be able to release small amounts from earmarked and restricted reserves as a one off contribution to protect general balances during the current year due to the pressure that the potential overspend could place on balances, but that it will still be necessary to budget for a contribution to balances during 2013-14, particularly if the overspend projected in 2012-13 remains at a high level.</p> <p>As always, these are figures which have to be kept under review in the light of changing circumstances, and which I will formally report on again as the Council sets the budget.</p>
<b>D – Recommendation</b>
None required – report for information at this stage

**Name of author of report – Gill Lewis**  
**Job Title –Interim Head of Function (Resources)**  
**Date – 23 November 2012**

<b>Appendices:</b>
Appendix A – Earmarked Reserves Appendix B – Restricted Service Reserves
<b>Background papers</b>
Cipfa LAAP Bulletin on Local Authority Reserves and Balances

Most years the aim is to balance the budget without drawing on reserves. This is what we did with general balances in the last four years:

YEAR	Original Budget	Revised Position in Adequacy of Reserves Assessment	Out-turn
<b>2009-10</b>	Recognising the deteriorating position but at that time expecting 2010-11 to be better, the Council's budget drew £1 million from general balances and nearly another £1 million from assorted earmarked reserves.	The monitoring report for 2009-10 suggested that not all the £1 million would in fact be drawn from general reserves, which was fortuitous given that the outlook for 2010-11 and subsequent year was now much worse	<b>£5.8m</b>  Increase of £1.1m in general balances as a result of the corporate budgets being underspent and there being some large windfall income; Waste budgets also continued to be under-spent.
<b>2010-11</b>	Minimal use of balances in main budget but with an approved contribution from balances of up to £0.6m to cover severance costs.	As a result of foreseen savings of £2.2m at the end of the third quarter boosting general balances above the required level, it was decided that up to £2.5m could be used in 2011/12 to cover severance costs.	<b>£6.7m [<del>£7.7m comparing like with like</del>]</b>  Savings of £2.5m set against 2010-11 severance costs of £0.6m. Net effect was increase of £1.9m in balances before applying a provision (a form of technical adjustment) of £1m to reflect projected severance costs. Those costs were defrayed in 2011-12.
<b>2011-12</b>	The projected improvement in 2010-11 lead to the general balances being above the level judged "adequate" and enabled the Executive to release up to £2.5 million to finance	Only about £1m of the £2.5m was required for severance in the main cuts programmes.  However the severance programme put additional	<b>£5.8m</b>  By the end of the year, the call on general balances had deteriorated

	severance costs. While this strategy was expected to leave the authority with adequate reserves by the end of 2011-12, there was danger of deterioration after that if other risks manifested themselves.	pressure on the key corporate services identified for capacity building. The Board of Commissioners on 14 November approved release of part of the surplus to correct this.  At the third quarter budget review an overall overspend of £0.7m was envisaged on net budgets, mitigated by a projected reduction in the cost of redundancies, reducing the call on general balances by £0.7m.	by £0.2m, mainly as a result of further costs from redundancies. However, the contribution from balances was £0.6m less than originally budgeted. The final out-turn for the year is a reduction of £0.9m in General Balances to £5.8m [reduction of £1.9m on like for like basis.]
<b>2012-13</b>	Release of £0.9m (together with £0.3m from earmarked reserves) to finance severance costs and other related one off costs. Given the scale of the budget savings and cuts, it was unlikely that £1.2m would be sufficient for this purpose and in order to avoid the situation where the one off cost of termination might be a barrier to achieving ongoing savings. As an exception to normal arrangements the Chief Executive as Head of Paid Services and in consultation with the s151 Officer authorised to release up to another £1m from balances for this purpose. Use of this £1m would bring the projected level of general balances down to a level of £4m by the end of 2012-13. This level is low in the context of the continuing economic pressures	Likely that the £1.2m released from reserves and balance will be required for severance.  The second quarter budget monitoring report indicates an overspend of £2.6m unless mitigating action is taken.	n/a

The second quarter monitoring statement indicated a potential deficit of up to £2.6m on the year. The extent of non achievement of this year's cuts programme had not been foreseen in the report on robustness of estimates and adequacy of reserves. There is also an unforeseen overspend on demand led budgets. This will, therefore, affect financial standing assessments in the current year, as well as being a setback on the savings programmes going forward.

The approach outlined here follows that adopted in recent years as part of the budget round, updated to take account of this year's projections.

As before, it is important to recognise that:-

- all reserves are in the ownership of the Council as a body corporate (except for schools reserves);
- some reserves are statutory and may only be spent as prescribed - e.g. school reserves, housing revenue account;
- some reserves represent commitments already made - e.g. capital expenditure reserve;
- some reserves represent funds already earmarked for a particular purpose by a decision of the Council;
- some reserves have been created by past decisions of the Council but are not earmarked to any particular purpose;
- the remainder of reserves can be a mixture of the above.

I begin by reviewing the financial reserves and provisions which were stated in the Council's balance sheet as at 31 March 2012. The latest position can be projected and compared with the liabilities or spending which have been, or may be, met from such reserves.

## **1. Schools' Balances**

At 31 March 2012 the total of schools' balances were £1.25m, a reduction of almost £1m during the year

The high level of schools' balances in total has been of some interest and controversy. Welsh Government published figures in October which showed that Anglesey's figures are now on average slightly lower than the average for Wales, having been for five years amongst the highest in Wales and one-and-a-half times the national average, both as a percentage of budget and per pupil.

The total reserves are now almost 3.4% of the total budgets, (down from 5.9%) but this conceals considerable variations with 14 schools being in deficit and five being in considerable difficulty with deficits over 5%. Anglesey now has the highest proportion of schools with negative reserves. The highest balances at individual schools are, by value, £0.53 million and, as a percentage of budget, 20%; seven schools had balances of 10% or more.

Actions have been agreed in the Estyn PIAP in relation to the financial management of schools to ensure that budgets are sustainable and work is being done by Education and Finance to review those schools with negative balances. However, the sums are generally available only to the individual schools to support their budgets, not to the Council as a whole. Recent guidance allows clawback from schools balances in restricted circumstances. Any reductions to the schools' quantum would also hit the schools in deficit.

## **2. Housing Revenue Account**

The Housing Revenue Account budget is likely to show a break-even position with balance being £250k approximately by year end because there is a significant revenue contribution to capital and this balance is driven more by the capital financing decision than on the revenue transactions. The reserve is not available to Council Fund services.

## **3. Earmarked Reserves (other than Service Reserves)**

Appendix A reproduces the figures and narrative on earmarked reserves as in the audited 2011-12 statement of accounts, with an update on the current position.

The latest review of these reserves shows limited scope for clawback to support next year's budget. The balances identified for closer review are:

- The Penhesgyn Waste Management Site Reserve – the balance of £886k is earmarked towards potential obligations connected with the landfill site, risks which are difficult to quantify. Reports in previous years advised that it might be possible to release part of the reserve but that a further evaluation of these risks and alternative means of meeting them should they materialise would be required before any part of the reserve could be released. This issue was discussed in detail with External Audit in finalising the 2011-12 accounts – they believe that the separate provision for aftercare of the site is £788k too low. We have advised in previous years that under the circumstances it would not be wise to release the reserve. The Wales Audit Office are continuing to review this area across all Welsh Councils and further advice may well be in place for closure of the 2012-13 accounts. Until we have an agreed position, no further release on this reserve is recommended.

- The insurance reserve has increased in recent years ( by £400k to £2,529k last year) as a result of successfully defending some large claims. There may be potential to release part of this fund or to prevent it increasing. In previous years, the advice has been that a review should be commissioned before any significant sum is released. The deteriorating financial standing may change the position. It should also be possible to reduce the budgeted annual contribution to the fund. The position has deteriorated recently with an announcement in November that MMI, the insurer of the Council's predecessor authorities, no longer foresees a solvent runoff. This will lead to partial clawback of paid claims. The first call for clawback is on this reserve.
- The Capital Expenditure reserve has been kept at about £1million by using the year end financing decision to allow the flexibility of carrying forward revenue contributions as well as capital funds. This allows the switching of resources between revenue and capital. As there are unallocated contingencies in this year's capital budget, a one off transfer of up to £1 million is possible.

The Equal Pay, Single Status and Job Evaluation Reserve is likely to be needed as the Council comes to decisions in this area. There are also decisions to be taken in relation to Equal Pay which may or may not lead to a request for permission to capitalise some part of any payments.

#### **4. Service Reserves (other than restricted service reserves)**

Service reserves are created when services underspend their annual budgets and carry forward the difference to be spent in subsequent years. Some services are in deficit to the extent that past overspending has not yet been paid back.

In early 2009 this approach was tightened by limiting the carry forward to 1% of budget, except where a commitment has been approved in advance. The Executive agreed to this approach to be applied to carry forwards as at 31 March 2010 and for future years. This approach leads to a balance of £1.5m in aggregate across services as at 31 March 2012, reducing as commitments unwind.

If the Executive wishes to tighten this situation in future years it is possible to amend the percentage that can be carried forward.

#### **5. Restricted Service Reserves**

These are mainly reserves created when money earmarked, often by third parties, for specific projects slip from one year to the next. Appendix B reviews the restricted reserves as at 31 March 2012.

There was clawback of £300k from these reserves last year. We are still discussing the detail but it seems that a small amount, say £100k, can be released this year.

I have requested a review of those restricted service reserves that appear to me to be less restricted in terms of the related grant conditions. I will report back on these in due course.

#### **6. Provisions**

The best assessment of financial standing is the extent to which the Authority has made provisions for known liabilities and the amount of distributable reserves available to cover other risks. For completeness, provisions are also disclosed here with the reminder that they have a very specific status in the Council's accounts as an item more akin to a commitment than the uncommitted and discretionary status of most reserves. They are discussed and agreed with the auditors who are able to request that the Council sets its provisions at a particular level. As at the balance sheet date, the following provisions had been made:

- Insurance Claims £253k
- Penhesgyn Waste Disposal Site £1,894k
- Termination Benefits £326k
- Other including Equal Pay £3,965k

## **7. General Revenue Balances**

The Council's general revenue balance as at 31 March 2012 stood at £5.80 million, in the Statement of Accounts and the budget for 2012-13 approved the use of £0.90 million of this, leaving a projected balance at year end of £4.90m. The report on the current year's revenue budget now projects a deterioration as a result of non achievement of efficiency savings, as well as overspends on demand led budgets. Efforts are being made to mitigate the overspend and make additional savings, however as we only have four months of the financial year remaining, pulling the spend into line is looking increasingly unlikely and there may still be a significant sum to address. There remains great uncertainty on current year budgets as a result of these issues. The revised projection for general balances is in the range £2.0 million to £2.5 million as at 31 March 2013 unless a transfer is made from earmarked reserves as outlined above.

A long term target of 5% of the net revenue budget excluding schools has been discussed in the past. In previous reports we have also outlined a risk-based approach which takes account of certain types of risk and their possible impact, building up to the amount required in a credible worst case. Both these approaches resulted in a figure in the region of £4 million. In February 2011, this figure was reviewed having regard to the higher level of funding risk inherent in medium term projections of public spending, and the higher level of optimism risk inherent in the Authority's budget. The professional advice at that time was that the figure should be increased to £4.5 million. By February 2012 that figure was set at £5m, with authorisation for the Chief Executive as Head of Paid Services and in consultation with the s151 Officer to release up to another £1m from balances for this purpose. It was noted that use of this £1m would bring the projected level of general balances down to a level of £4m by the end of 2012-13 and that level is low in the context of the continuing economic pressures.

## **8. Conclusion**

To assist in budget planning, I can advise the Executive that they may be able to release small amounts from earmarked and restricted reserves as a one off contribution to protect general balances during the current year due to the pressure that the potential overspend could place on balances, but that it will still be necessary to budget for a contribution to balances during 2013-14, particularly if the overspend projected in 2012-13 remains at a high level.

The Senior Leadership Team and Finance Officers will review the position and feed into future advice. As always these are figures which have to be kept under review in the light of changing circumstances, and which I will formally report on again as the Council sets the budget.

## EARMARKED RESERVES

RESERVES	AMOUNT 31-03-12 £'000	STATEMENT OF ACCOUNTS NARRATIVE 2011-12	FURTHER COMMENTS
<b>Capital Expenditure</b>	1,000	To fund capital expenditure in future years. This has been created to ensure committed capital expenditure, including expenditure which has slipped from previous years, is fully financed.	Spent or still committed to capital slippage and budgets in the 2012-13 capital plan. Could be clawed back with corresponding reduction in unallocated capital budgets.
<b>Penhesgyn Waste Landfill Site Reserve</b>	886	This reserve has been created from the net cash assets, less winding up and capping costs, of Cwmni Gwastraff Môn-Arfon Cyf which is in the process of being wound up. The reserve will be used to contribute towards any future liabilities arising from the management of the Penhesgyn site.	There are a number of potential liabilities arising from the ownership of the site which have not been formally provided for. This reserve covers a proportion of those potential liabilities including the £788k referred to by the External Auditor in their ISA 260 report on the Accounts.
<b>Infrequent Events</b>	30	to allow the Council to even out from year to year the cost of making contributions to events which occur less frequently than annually.	£20k spent on Olympic flame celebration. Still useful but not required.
<b>Museum Purchases</b>	15	Earmarked gifts and other finances to fund future expenditure of Oriel Ynys Môn.	Still required.
<b>Leisure Improvements Reserve</b>	215	To fund capital expenditure on improvements to, and provision of, strategic leisure facilities.	This has been partly allocated by the Board of Commissioners. Would require a decision of the County Council to release for other purposes.
<b>School Days</b>	(19)	To equalise the costs of varying number of school days in each financial year.	Still required.
<b>Service Reserves</b>	1,507	Under the Council's Financial Procedure Rules over and under-spending is carried forward as earmarked reserves to the level set by the Executive.	This is the balance with the limit set at 1% of budget plus approved commitments. It is reduced by £400k from 2011, and is likely to be further reduced by year end. Should be reviewed for 2013-14.
<b>Restricted Service Reserves</b>	1,781	Earmarked budgets within service areas which remain unspent at year end.	Appendix C.
<b>Building Maintenance Service</b>	81	To provide a working balance. A substantial part of this balance accrued under the Unit's previous status as a Direct Service Organisation under Compulsory Competitive Tendering legislation.	Still required but may be reviewed as part of current review of the service.

RESERVES	AMOUNT 31-03-12 £'000	STATEMENT OF ACCOUNTS NARRATIVE 2011-12	FURTHER COMMENTS
<b>Equal Pay, Single Status and Job Evaluation</b>	1,966	As a result of the 'Single Status' agreement, the Authority, in common with most other local authorities, is required to introduce a new pay and grading system with effect from 1 April 2007. The extent to which this may involve an obligation to back pay is uncertain. Negotiations are proceeding on a revised pay and grading structure. A sum has been set aside in the Job Evaluation reserve towards the overall cost of the exercise, including the administrative costs, the cost of new pay scales, any pay protection and any back pay. Although the individual elements cannot be estimated with certainty, the Authority is of the view that the sums set aside are adequate.	Decision of Pay and Grading Panel, October 2009 and Executive, November 2009 fully commit this towards protection and other costs of the grading review.
<b>Section 118 (Mental Health Act 1983)</b>	299	To provide for the anticipated repayment of charges previously levied on some Social Service users.	Known cases could make a substantial call on this and there remain other potential claims.
<b>Recycling</b>	1,473	Landfill cost savings created by diverting waste to recycling. The reserve will be utilised towards recycling initiatives.	Committed by waste grant conditions and past Executive decisions to recycling. Projects approved by Commissioners. The reserve includes £312k for income related to recycling. WG guidance is that this income is also tied by the terms and conditions of the grant.
<b>Risk Management Reserves</b>	65	the Risk Management Reserve was set up to cover work done in collaboration with the Council's Insurers including Corporate Risk Management, Business Continuity and Health and Safety.	Contractually committed.
<b>Performance Management Reserves</b>	1,054	Amounts earmarked towards performance improvement measures from the Outcome Agreement Grant.	This comprises Performance Incentive Grant (now Outcome Agreement Grant received up to 2011-12; all of which has now been allocated. Earmarked as a source of funding for recovery and improvement work this year, as in previous years.
<b>Insurance</b>	2,529	The Council runs an internal insurance account which pays for self insured losses and which receives 'premia' from service accounts. The known losses at year end are provided for. This reserve is the surplus on the internal insurance account plus interest on balances and is intended to cover claims which have been incurred but have not been reported.	<p>Already reduced by £0.4m as part of 2009-10 budget plan, but balance has increased again.</p> <p>However claims experience has deteriorated in some areas and an actuarial assessment would be useful before clawing back. Consider reducing the annual contribution.</p> <p>On 13 November, there was an announcement that MMI, the insurers of predecessor authorities was entering administration. This is likely to mean claw-back of claims previously paid.</p>



## RESTRICTED SERVICE RESERVES

RESERVE	£'000	PURPOSE OF RESERVE	COMMENT/UPDATE
<b>Cost of Change</b>	172	Expenditure in preparation for Affordable Priority Programme Projects.	Offset against savings in current and future years.
<b>Oriel Ynys Môn – Llyn Cerrig Bach</b>	4	To fund costs of project.	Still required.
<b>R &amp; M Schools</b>	20	To smooth out costs of schools R & M.	Offset against service reserve.
<b>School Breakfast Set up Cost</b>	37	Balance of Welsh Assembly Government Grant. Used to fund the set up costs for any school where a Breakfast Club is set up.	Still required – grant conditions.
<b>Sickness Absence Scheme</b>	120	Used to fund the cost of supply if teachers are absent through sickness. Schools pay a premium from their budgets each year and costs are funded from these premiums. This reserve represents the net balance of premiums paid over costs incurred.	Still required.
<b>Risk Management</b>	58	Balance of the unused budget from the Corporate Risk Management Budget.	Mostly still required – clawback taken in 2012-13.
<b>Strategic Development Scheme</b>	113	Committed to fund grants already awarded on SDS scheme where the project has yet to be carried out.	Mostly still required – clawback taken in 2012-13.
<b>Licensing</b>	23	Due to cyclical nature of the licences issued, it is projected that the administrative work will be higher every fifth year. Reserve will meet the additional costs in those peak years.	
<b>Mobile CCTV</b>	12	Specific Grant.	Still required.
<b>Maes Awyr Môn</b>	21	Balance of funding received to set up airport. Earmarked to be used to meet any future costs relating to the airport.	Still required.
<b>South Stack</b>	14	To fund future maintenance costs of South Stack.	Still required.
<b>Capacity Fund</b>	80	Balance of unspent budgets from 2010-11.	Being used this year.
<b>Child Protection Board Reserve</b>	24	Balance of unspent budgets from previous years. Will be used to fund costs of the Board which are in excess of the budget in future years.	Still required.
<b>NWW Treatment Plant</b>	535	Unspent budgets.	Still required to cover commitment.
<b>Energy Island</b>	235	Unspent contributions: Council and Third Party.	Carries forward unspent budgets.
<b>Client's funds</b>	43	Clients' funds.	To be re-designated.
<b>Decommitted</b>	252	Various de-committed or re-designated	To be re-designated or given up.
<b>Supporting People</b>	2,074	Unspent amounts set aside for activities related to the programme	Re-designated in 2012-13. To be reviewed.