

## APPENDIX 4

### Reserves Policy 2024/25

#### Middlesbrough Council

##### 1. Background

- 1.1. The Council is required to maintain adequate financial reserves. Reserves are an integral part of sound financial management, they help the Council plan for future spending commitments, balance the budget and manage unpredictable financial pressures.
- 1.2. Sections 32 and 43 of the Local Government Finance Act 1992 require councils to consider the level of reserves when setting a budget requirement. Section 25 of the Local Government Act 2003 requires the Chief Financial Officer (Section 151 Officer) to report formally to Council on the adequacy of proposed reserves when setting the budget and council tax requirement. This is completed at the Council through the Robustness Statement. The accounting treatment for reserves is set out in the Code of Practice on Local Authority Accounting.
- 1.3. CIPFA issued [Local Authority Accounting Panel \(LAAP\) Bulletin No.99](#), Guidance Note on Local Authority Reserves and Balances in July 2014. CIPFA also issued [CIPFA Bulletin 13 Local Authority Reserves and Balances](#) on 28 March 2023. Compliance with the guidance is recommended in CIPFA's Statement on the Role of the Chief Financial Officer in Local Government. In response to the above requirements, this policy sets-out the Council's approach for compliance with the statutory regime and relevant non-statutory guidance for the Council's cash backed usable reserves.
- 1.4. All reserves will be categorised as per the Local Authority Accounting Practice guidance, into groupings.
- 1.5. Within the Statement of Accounts for General Fund Earmarked Reserves, all individual reserves are reported and will include a description of the purpose of the reserve.
- 1.6. Earmarked reserves will be reviewed regularly as part of the in-year monitoring and accounts closure process and annually as part of the budget setting process, to determine whether the original purpose for the creation of the reserve still exists and whether or not the reserves should be released in full or in part or require topping up based on known/expected calls upon them.
- 1.7. Particular attention will be paid in the annual review to those reserves whose balances have not moved over a two-year period, other than the General Fund, for further detail see Section 4 Management and governance.



<p><b>Earmarked Reserves (unusable)</b></p> <p><b>Annex B</b></p>	<p>These arise out of a requirement under legislation and proper accounting practice either to accumulate revaluation gains or as adjustment accounts to comply with statutory accounting requirements. These reserves are not backed by cash resources and therefore cannot be used for any other purpose. Hence, these reserves are not available to fund expenditure. These will generally be excluded from any discussion where the Council talks about its level of reserves.</p>
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1.9 The Chartered Institute of Public Finance and Accountancy (CIPFA) recommend that the following factors should be taken into account when considering the level of reserves and balances:

- Assumptions regarding inflation and interest rates.
- Estimates of the level and timing of capital receipts.
- The capacity to manage in-year demand led pressures.
- Ability to activate contingency plans if planned savings cannot be delivered.
- Risks inherent in any new partnerships.
- Financial standing of the authority (level of borrowing, debt outstanding etc.)
- The authority's record of budget management and ability to manage in year budget pressures.
- Virement and year-end procedures in relation to under and overspends.
- The general financial climate.
- The adequacy of insurance arrangements.

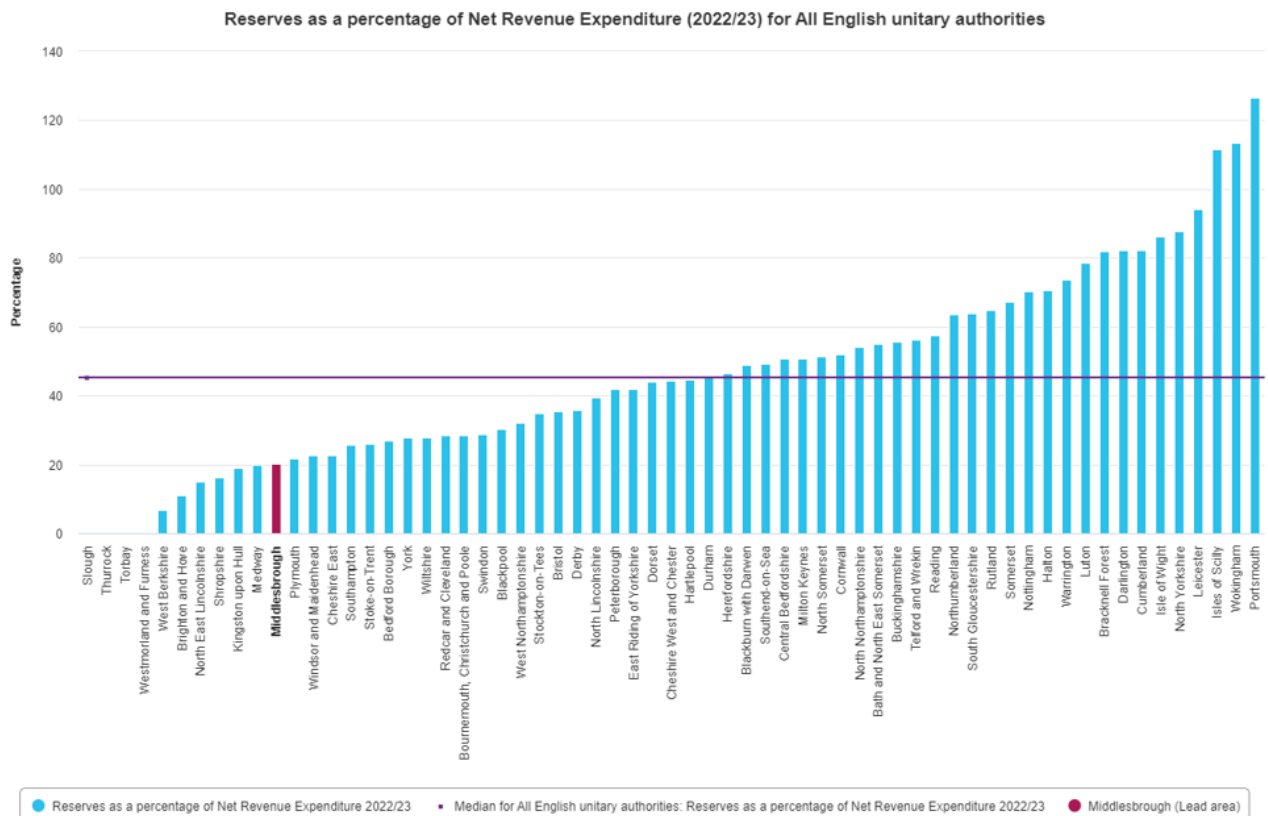
1.10 Each local authority must make its own decisions about the level of reserves it hold, taking into account all of the issues referred to above and the advice of the s151 Officer. The level of the general fund reserve will be a matter of judgement which will take account of the specific risks identified through the various corporate processes. It will also take account of the extent to which specific risks are supported through earmarked reserves.

1.11 The Council earns interest on the investment of its cash balances through its Treasury Management operations. This revenue income supports its general spending plans. By holding cash balances, the Council effectively internalises some of its borrowing, therefore avoiding interest charges on external debt. Balances held in reserves therefore help to reduce on-going revenue expenditure.

## **2 Strategic Context**

2.1 The Council is facing a shortfall in funding compared to the level of service demand that it is experiencing. It must urgently review its priorities and redesign and transform its services over the period of the MTFP to deliver cost reduction and efficiency to achieve a budget that is financially sustainable over the medium term.

- 2.2 To achieve financial sustainability, the Council will need to invest in a range of innovative and transformational activities in order to reduce future costs of service delivery. The Council's earmarked revenue reserves are at a critically low level and therefore are not sufficient to fund this innovation and transformation. The primary source of funding for transformation will be to generate a pipeline of capital receipts from asset sales and apply them to fund transformation in accordance with the Flexible Use of Capital Receipts (FUoCR) Strategy in accordance with Government regulations. The Council has no unapplied capital receipts forecast to be in the bank at 1 April 2024.
- 2.3 The Council is in the process of reviewing its asset base and a plan for asset rationalization was approved by the Executive in November 2023. This has resulted in an Asset Disposal Programme that will be managed as part of the Council's Transformation Programme. The Asset Disposal Programme is fundamental to the Council's ability to successfully deliver transformation.
- 2.4 Over the term of the MTFP, the Council will need to maintain a minimum General Fund Balance and to replenish and maintain an increased level of earmarked revenue reserves in order to improve its financial resilience. At the end of 2022/23 financial year, the Council has one of the lowest levels of total reserves as a proportion of net revenue budget compared to all unitary councils as illustrated below.



Source: LG Inform

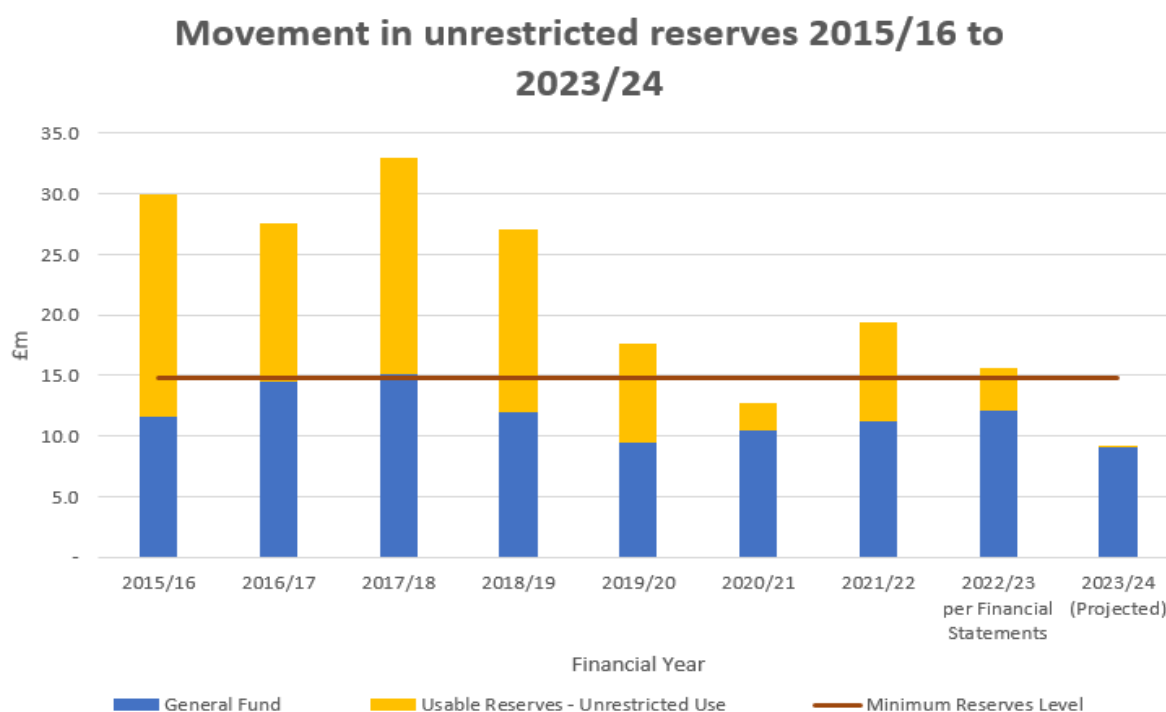
### **3 Management and governance**

- 3.1 New reserves may be created at any time and approved by the Executive upon recommendation by the s151 Officer.
- 3.2 For each earmarked reserve held there will be a clear protocol setting out:
- The reason for/purpose of the reserve
  - How and when the reserve can be used
  - A profile over which the reserve is intended to be utilised showing expected contributions to and from the reserve, with an end date for its existence.
- 3.3 The s151 Officer shall approve the draw down of reserves provided that they are for the purpose for which the reserve has been established. The use of reserves will be reported as part of the quarterly budget monitoring report to the Executive.
- 3.4 The s151 Officer will review the use of reserves in accordance with the planned profile periodically through the financial year and as a minimum at accounts closure and budget setting. Protocols will be updated as appropriate.
- 3.5 All protocols will have an end date and at that point any balance will be transferred to the general reserve. If there is a genuine reason for slippage, then the protocol will be updated and submitted through Financial Planning for agreement by the S151 Officer or referred to the Executive as appropriate.
- 3.6 Ongoing recurring costs should not be funded from reserves unless part of a smoothing reserve and approved as part of the MTFP. The short-term use of reserves may be agreed to provide time to plan for a sustainable funding solution in the following financial year. Decisions on the use of reserves may be delayed until financial year-end and will be dependent on the overall financial position of the Council rather than the position of just one service area or directorate.
- 3.7 Council will consider a report from the s151 Officer on the adequacy of the level of reserves as part of the annual budget-setting process.
- 3.8 The Council will review and update the Reserves Strategy and Policy annually as part of the budget setting process.

### **4. Level of General Fund Balance Usable Reserves**

- 4.1 Over recent years the level of the total value of the Council's Unrestricted usable reserves and General Fund Balance have declined as shown in the Graph below. This has weakened the Council's financial resilience in terms of its ability to be able to respond to unforeseen cost pressures and has left the Council in a financially fragile position during 2023/24 given the unprecedented levels of demand and complexity for statutory services being experienced following the Covid-19 pandemic.

- 4.2 At the start of 2023/24 the General Fund Balance was £12.041m (9.5% of NRB) and the level of the Council’s earmarked unrestricted reserves at £2.788m was described as ‘critical’ by the s151 Officer and the requirement for robust cost control and savings delivery was essential to protecting those reserves at a minimum of £14.829m.
- 4.3 Based upon the forecast outturn at Quarter 3 (ending 31 December 2023) the forecast balance on the unrestricted usable reserves is £0.055m and on the General Fund Balance is £9.036m. This is below the minimum level set at the start of 2023/24, due to expenditure pressures that have proved difficult to mitigate in year in relation to Adults and Children’s social care and SEND transport.



- 4.4 The s151 Officer has undertaken an in-depth review of the balance sheet during the 2023/24 financial year to assure the correct classification of amounts held in the General Fund Balance sheet. In addition, a review of the methodology for calculating the Collection Fund bad debt provision from 2021/22 accounts which remain subject to the conclusion of the external audit. Together with the 2023/24 forecast outturn on the Collection Fund, this has resulted in a cumulative surplus of c£8.3m being available for the General Fund to precept at budget setting 2024/25. The surplus will be applied to rebuild the General Fund Balance and earmarked unrestricted usable reserves to rebuild financial resilience and is not therefore available to balance the 2024/25 budget.

### General Fund Balance

- 4.5 The level of the General Fund Balance is a matter for the Council to determine having had regard to the advice of the s151 Officer. A general assumption over many years was to allow for a minimum balance of 5% of Net Revenue Expenditure. However, due to the increasing financial risks and uncertainties facing local

authorities over the period since austerity in 2008/09, the minimum average balance recommended by s151 Officers has tended to increase. It is now more usual for a minimum of around 7.5% being held by many authorities together with substantial earmarked reserves that are necessary to manage risk and uncertainty around future government funding and increasing demand and cost of adults and children's services and SEND transport for which the Council has statutory duties that must be met.

- 4.6 The s151 Officer recommends that the General Fund Balance should be maintained at a minimum of 7.5% of the Net Revenue Budget over the period of the MTFP to 2026/27 as follows:

Year	Forecast Contribution to General Fund £m	Forecast General Fund Balance £m	Forecast NRB £m	Reserve to NRB %
2023/24	0.000	9.000	126.354	7.1
01-Apr-24	2.100	11.100	147.890	7.5
2024/25	0.000	11.100	147.890	7.5
2025/26	0.000	11.100	148.601	7.5
2026/27	0.000	11.100	148.127	7.5

### Financial Resilience Reserve (FRR)

- 4.7 The s151 Officer recommends that in addition to 7.5% NRB for the General Fund Balance, a Financial Resilience Reserve be rebuilt and maintained to a target value of between £8m to £10m over the period of the MTFP to March 2027 in order to strengthen the Council's financial resilience. This is based upon sensitivity analysis upon the budgeted pressures included in the 2024/25 MTFP model.

	2024/25 MTFP Changes £m	2024/25 FRR	2025/26 - 2026/27 FRR	
		Requirement £m	Minimum Requirement £m	Maximum Requirement £m
Service Demand Pressures	20.764	2.481	5.994	7.649
Pay Award Increase	3.556	0.889	0.889	0.889
Contractual Inflation	1.550	0.155	0.465	0.620
Income Inflation	(1.853)	0.093	0.556	0.741
Shortfall on Capital Receipts	0.000	0.600	0.000	0.000
	<b>24.017</b>	<b>4.217</b>	<b>7.904</b>	<b>9.899</b>

- 4.8 The purpose of the Reserve will be to manage the volatility of actual income and expenditure against budget estimates without calling upon the General Fund Balance given the uncertain environment within which the Council is managing its operations. The budgeted contributions to the FRR over the period are summarised below. Any drawdown from the FRR in year will be required to be budgeted to replenish the FRR in the following financial year. Any underspend at final outturn will be transferred into the Council's Financial Resilience Reserve unless otherwise recommended by the S151 Officer.

Year	Forecast Contribution to £m	Forecast Contributions (from) £m	Forecast FRR Balance £m
2023/24		(1.798)	NIL
01-Apr-24	3.320	-	3.320
2024/25	1.441	-	4.761
2025/26	1.250	-	6.011
2026/27	2.000	-	8.011

### Change Fund Reserve

- 4.9 The Council holds a Change Fund Reserve for the purpose of meeting the revenue costs of transformation and efficiency programmes, including meeting redundancy costs. The Council is embarking upon a major Transformation Programme that will run for two to three years from 2024/25. Whilst the main source of funding will be the Flexible Use of Capital Receipts (FUoCR), there are some costs which are not eligible to be capitalised under the FUoCR regulations and therefore they will be funded from this Reserve.

Year	Forecast contribution to £m	Forecast contribution from £m	Forecast Change Fund Balance £m
2023/24	1.487	(1.487)	NIL
01-Apr-24	1.000	-	(1.000)
2024/25	0.730	(1.730)	NIL
2025/26	0.730	(0.730)	NIL
2026/27	0.730	(0.730)	NIL

### Savings Delivery Risk

- 4.10 The scale of the Council's 2024/25 to 2026/27 presents a significant challenge for which appropriate Transformation and Programme Management Governance arrangements are being established in order to secure successful delivery. Prudent financial provision would normally be made in earmarked revenue reserves to offset the risk of slippage / non delivery. However, the Council holds insufficient levels of reserves to make appropriate financial provision for this risk. Therefore, the Council's application for Exceptional Financial Support from DLUHC includes a request to capitalise up to £3.5m of savings slippage in 2024/25 in the event that savings are not realised at the required pace during 2024/25.



## **Legacy Accounts and Audit Reserve**

4.11 The Council currently has prior years Statements of Account that remain subject to the completion of the external audit, with the delay due largely to the impact of the national reset of the local authority audit market by DLUHC. DLUHC is currently consulting between 8 February and 7 March 2024 in relation to arrangements for re-setting the local authority audit market and the prospect of local authority accounts being subject to qualification or disclaiming (not being audited) by the external auditor as part of the approach to clear the backlog of legacy accounts up to 2022/23 by 30 September 2024. Officers will discuss with the auditor once they set out their proposals for concluding the 2021/22 and 2022/23 audit for Middlesbrough in light of the consultation. An earmarked reserve of £1m has been set aside to provide for unforeseen adverse audit adjustments that may arise from the conclusion of these legacy audits in future periods.

## **5. Summary of forecast revenue reserves**

5.1 The critically low level of revenue reserves advised to the Council at budget setting in March 2023 have been further depleted as a result of the continued expenditure pressures which Service Directors have been unable to control whilst operating under their current arrangements. The forecast level of reserves of £9.091m at 31 March are insufficient and would have resulted in the s151 Officer needing to issue a s114 Notice in 2023/24 if it had not been possible to identify a solution.

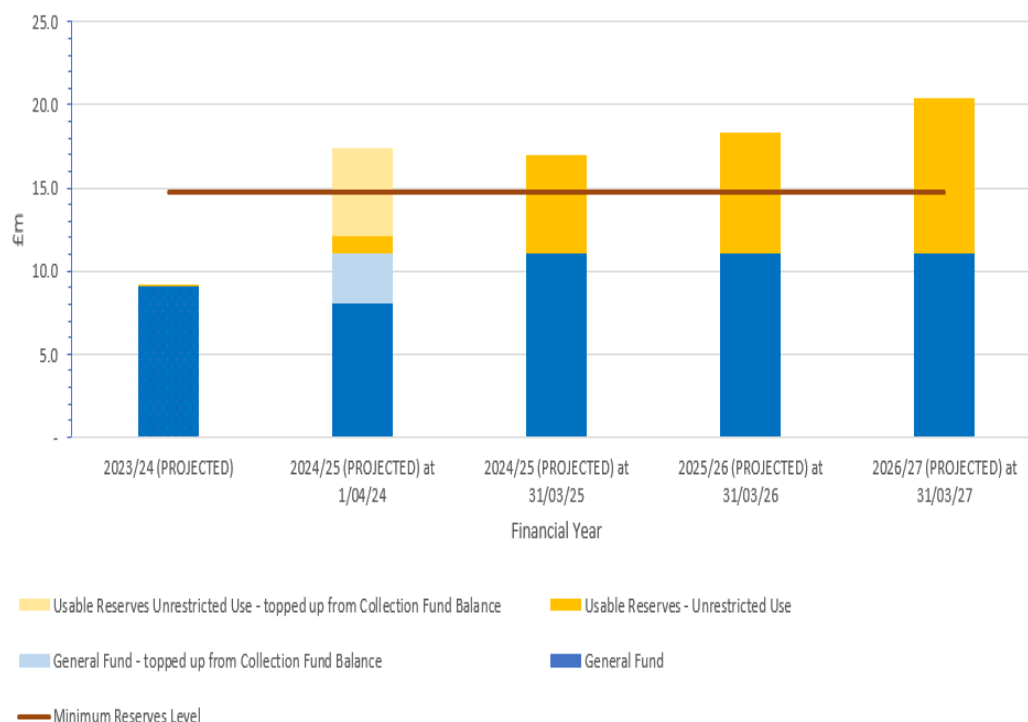
5.2 The detailed review of the balance sheet identified the need to review and apply a one off and exceptional adjustment of £8.3m to the Collection Fund Bad Debt provision resulting from the application of the accounting methodology to comply with accounting standard IAS37. This provides a solution to restore unrestricted usable revenue balances to the level of £17.4m. Revenue reserves will be replenished by the application of the forecast Collection Fund surplus of c£8.3m on 1 April 2024.

5.3 As a result of these actions and a review of the Reserves Policy, the minimum level of the General Fund Balance will be set at a minimum of 7.5% of the Net Revenue Budget equivalent to £11.1m for 2024/25.

5.4 The Council must aim to rebuild its unrestricted revenue reserves over the period of the MTFP. The balance on earmarked unrestricted reserves at 1 April 2024 is expected to be £6.3m

5.5 Within unrestricted revenue reserves, the Financial Resilience Reserve (FRR) will operate as a budget smoothing reserve to meet unanticipated financial pressures subject to recommendation by the s151 Officer to the Executive. The FRR is required to be rebuilt and maintained at between £8m to £10m by 2026/27 to provide sufficient resilience to support the management of risks in the delivery of the revenue budget over the period.

### Projected Unrestricted Reserves Balances from closing balance 2023/24 through to closing balance 2026/27



The projected balances on reserves as at 31/03/24 is as below:

	£m	£m
<b>General Fund Reserve</b>		<b>9.036</b>
<b>Usable Earmarked Reserves</b>		
Restricted Use	2.121	
Unrestricted Use	0.055	
	<hr/>	<b>2.176</b>
<b>Unusable Earmarked Reserves</b>		
Dedicated Schools Grant Adjustment Account	(13.208)	
Schools Balances	3.641	<b>(9.567)</b>
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		<b>1.645</b>

## Annex A – General Fund & Earmarked Reserves

The Council holds a number of usable reserves, and these are listed below.

Reserve	Description
General Fund Balance	<p>This Fund is the statutory fund into which all the receipts of the Council are required to be paid in, and out of which all liabilities of the Council are to be met, except to the extent that statutory rules might provide otherwise.</p> <p>This is a minimum balance which is a contingency to cushion the impact of unexpected events or emergencies. This is the fund of last resort. This reserve ultimately smooths the financial impact of unexpected events, major incidents and unforeseen risks.</p>
Capital Receipts Reserve	This reserve holds amounts received from the disposal of assets and is only available to fund future capital projects.
Capital Grants and Contributions Unapplied Reserves	These reserves hold amounts from Capital Grants and Contributions that have been recognised in the Comprehensive Income and Expenditure Statement in line with the accounting code of practice, but for which the associated capital expenditure has not yet been incurred.

### Earmarked Reserves

Reserve	Description
Schools Balances	This reserve holds the accumulated balances and the differences between the school budget and actual expenditure incurred in the year for all the Middlesbrough Council schools. In accordance with Government regulations and the Council's scheme of delegation for schools, these funds are carried forward and specifically earmarked for use by schools in future years.
Public Health	The Public Health Grant received by the Council is ring-fenced for use on public health services only. This reserve is for any amounts of grant not spent in year due to timing differences in service delivery.
Insurance Fund	The internal Insurance Fund was set up to cover all the Council's insurable risks. Only a limited amount of external insurance cover is provided for catastrophe or special risk incidents. The nature of the risks covered by the insurance reserve include fidelity guarantee, personal accident, employers' liability, fire, motor, marine, engineers, public liability and money losses.

Better Care Fund	<p>The Better Care Fund (BCF) has been established by the Government to provide funds to local areas to support the introduction of a fully integrated health and social care system. It is a requirement of the BCF that the Clinical Commissioning Group (CCG) and the Council establish a pooled fund for this purpose.</p> <p>Section 75 of the National Health Service Act 2006 gives powers to local authorities and CCGs to establish and maintain pooled funds to support the outcomes of the BCF.</p> <p>The Council has entered into a pooled budget arrangement with NHS Tees Valley Clinical Commissioning Group for the provision of health and social care services to meet the needs of the population of Middlesbrough. The services being commissioned or provided by the Council or Tees Valley Clinical Commissioning Group (TVCCG) depend upon the needs of the service recipient. The Council and TVCCG have an ongoing section 75 agreement in place for funding these services and this is reviewed annually. The Council is the host for this pooled budget and each partner's contribution is set out in the Better Care Fund section 75 agreement.</p> <p>This reserve is to hold balances from the pooled budget.</p>
Revenue Grants Unapplied	<p>In situations where there are no grant conditions or that conditions have already been met and expenditure has not yet taken place, any unspent grants/contributions are transferred to the Revenue Grants Unapplied at year-end. These have been recognised as income in prior years in the Comprehensive Income &amp; Expenditure Statement.</p>
Marton Library Section 106	<p>This reserve is held for the purpose set out in the Section 106 agreement.</p>
Housing Rental Sinking Fund	<p>This reserve is for the replacement of major capital expenditure, e.g., replacement windows and boilers, for properties owned by the Council and rented out.</p>
Financial Resilience Reserve	<p>The purpose of the Reserve is to meet unforeseen financial pressures that cannot ultimately be managed within directorate budgets.</p>
Change Fund	<p>The reserve has been set up to pay for the one-off costs associated with implementing change within services including the funding of invest to save projects, early retirements / voluntary redundancies and altering the way services are commissioned.</p>
Car Parking Reserve	<p>This reserve was created from other reserves to cover potential pressures relating to car parking income arising in future years due to the on-going impact of Covid.</p>
Elections Costs	<p>This reserve covers the cost of elections which occur every four years, The reserve is built up with a contribution from the elections budget each year, and then drawn down in the fourth year when local elections take place.</p>
Legacy Accounts Reserve	<p>This reserve has been created to cover potential outstanding legacy audit adjustments required to the accounts once outstanding audits for previous financial years have been completed.</p>

## Annex B – Unusable Reserves

Unusable Reserves are those reserves held by the Council that cannot be utilised to provide services. This includes reserves that hold unrealised gains and losses and adjustment accounts which deal with situations where income and expenditure are recognised statutorily against the General Fund balance on a different basis from that expected by accounting standards as adopted by the Code. Unusable reserves cannot be used to fund expenditure e.g., cannot fund revenue spend on services or capital spend on projects.

Reserve	Description
Revaluation Reserve	<p>The Revaluation Reserve contains the accumulated net gains made by the Council arising from increases in the value of its Property, Plant and Equipment. The reserve only contains revaluation gains accumulated since 1 April 2007, the date when the Revaluation Reserve was constituted. Accumulated gains and losses accumulated before that date are consolidated into the Capital Adjustment Account. Amounts contained within this reserve will only become available to provide services (or limit resources in the case of losses) once the gains/losses are realised as the assets are disposed of.</p>
Capital Adjustment Account	<p>The Capital Adjustment Account absorbs the timing differences arising from the different arrangements for accounting for the consumption of non-current assets and for financing the acquisition, construction or enhancement of those assets under statutory provisions. The Account is debited with the cost of acquisition, construction and enhancement as depreciation, impairment losses and amortisations are charged to the Comprehensive Income and Expenditure Statement (with reconciling postings from the Revaluation Reserve to convert fair value figures to a historical cost basis). The account is credited with amounts set aside by the Council as finance for the costs of acquisition, construction, and enhancement.</p> <p>The Account also contains accumulated gains and losses on Investment Property and gains recognised on donated assets as well as revaluation gains accumulated on Property, Plant and Equipment before 1st April 2007, the date that the Revaluation Reserve was created to hold such gains.</p>
Deferred Capital Receipts	<p>Deferred Capital Receipts are amounts that are to be received in instalments over an agreed period of time. They arise from mortgages on the sale of Council Houses, or repayment terms from other asset sales. These can only be used for financing new capital expenditure when the actual receipt is received. When the deferred cash settlement eventually takes place, amounts are transferred to the Capital Receipts Reserve.</p>
Financial Instrument Adjustment Account	<p>This Account is held in accordance with the Code of Practice to write down over time the premiums paid on early debt repayment in order to spread the burden on Council Tax. This is a technical adjustment and has no impact on the overall financial position of the Council.</p>

Pension Reserve	This reserve is used to reconcile the payments made for the year to various statutory pension schemes and the net change in the Council's recognised liability under IAS19 – Employee Benefits, for the same period.
Collection Fund Adjustment Account	The Collection Fund Adjustment Account holds the differences arising from the recognition of council tax and business rates income, in the Comprehensive Income and Expenditure Statement as it falls due from council tax payers and business rate payers compared with the statutory arrangements for paying across amounts to the General Fund from the Collection Fund.
Accumulating Compensated Absences Adjustment Account	The Accumulated Compensated Absences Adjustment Account reflects the value of compensated absences (employees time off with pay for holidays) earned but not taken in the year.
Dedicated Schools Grant Adjustment Account	From November 2020 The Local Authorities (Capital Finance and Accounting) Regulations (the 2003 Regulations) established new accounting practices in relation to the treatment of local authorities' schools budget deficits such that where a local authority has a deficit on its schools budget relating to its accounts for financial years from 1st April 2020, it must not charge the amount of that deficit to a revenue account. The local authority must record any such deficit in a separate account established solely for the purpose of recording deficits relating to its school's budget. The CIPFA local authority accounting code has determined this as the 'Dedicated Schools Grant Adjustment Account'. The new accounting practice has the effect of separating schools budget deficits from its General Fund revenue budget.