

Appendix B

Minimum Level of General Reserves

1. **BACKGROUND INFORMATION**

- 1.1 As part of their annual budget setting process, Taunton Deane Borough Council and West Somerset Council reviewed and determined a minimum level of General Reserves. A similar review therefore needs to be undertaken for the new Somerset West and Taunton Council.
- 1.2 This review of General Reserves is essential particularly with this being the first year of operation of the new council and with the continued uncertainty over future Central Government Funding. In addition all councils are always exposed to unforeseen events, risks and pressures.
- 1.3 With this in mind, the s151 Officer has requested a review of reserves and for the minimum acceptable level of General Reserves to be challenged to establish whether it is appropriate and to benchmark against other councils to see how we compare and whether we are over exposed to risk.

2. **APPROACH AND METHODOLOGY**

- 2.1 Reserves will be reviewed by Somerset West and Taunton Council on an annual basis to give assurance that they are appropriate and adequate. Due to the constraints on the Council's budget it is not possible to mitigate against every eventuality and it would be imprudent to set aside funds simply as a percentage of net expenditure or "just in case". With the challenges associated with setting a balanced budget, earmarking reserves is an important exercise and each year a review is done to challenge the levels and intended use of these reserves. In some cases, where earmarked reserves are deemed to be no longer required/too high they can be returned to general reserves.
- 2.2 In order to arrive at an appropriate level, various publications are reviewed and the Council will benchmark against its nearest neighbours in terms of size, demography, NDR value per head etc*:
 - LAAP Bulletin 99 Local Authority Reserves and Balances
 - CIPFA Stats Nearest Neighbours Model*
 - Audit Commission "Striking a Balance" Questionnaire
 - CIPFA Delivering Good Governance in Local Government

3. **MITIGATING RISK – GENERAL RESERVES**

- 3.1 The CIPFA LAAP Bulletin says "When reviewing their medium term financial plans and preparing their annual budgets, local authorities should consider the

establishment and maintenance of reserves. These can be held for three main purposes”:

- A working balance to help cushion the impact of uneven cashflows and avoid unnecessary temporary borrowing – this forms part of general reserves
- A contingency to cushion the impact of unexpected events or emergencies – this forms part of general reserves
- A means of building up funds to meet known or predicted requirements – via earmarked reserves (legally part of the General Fund)

3.2 As part of the review of the adequacy of the General Reserves balance it is prudent to consider the particular risks that the Council faces and how these are mitigated by earmarked reserves and other mechanisms.

3.3 There are a number of general risks which are relevant to all or most councils and for the most part are mitigated with a robust approach to budget setting in the MTFP. These include inflation and interest rates; the timing of capital receipts; demand led pressures; the delivery of efficiency savings; the availability of Government grants and general funding and the general financial climate. These risks are considered at every stage of the budget setting process and the experience of the s151 and senior finance officers will be fundamental in identifying and addressing the pressures relating to these risks.

3.4 An indicator of the risks particular to the Council is the Risk Register. This captures those risks which need to be managed and monitored as they can potentially have a very detrimental effect on the financial or reputational standing of the Council. We have therefore used the Council's risk register as the starting point for the risk matrix.

4. QUANTIFYING THE FINANCIAL RISK

4.1 The risk-based assessment gave a range of appropriate “minimum” general reserves levels as £1.9m to £2.9m. With consideration to the challenges the Council faces from continuing reductions of Central Government funding and a need to deliver its transformation savings it is prudent to recommend that the minimum reserve level for the new council be set at £2.4m.

5. STRIKING A BALANCE QUESTIONNAIRE

5.1 The Audit Commission's questionnaire is a good aide memoire to highlight the areas a Council should consider when assessing the minimum level of reserves. It also draws on benchmarking to establish how other councils mitigate their risks.

6. NEAREST NEIGHBOUR COMPARISON

- 6.1 A benchmarking exercise with 15 other councils with similar attributes has been undertaken. The nearest neighbour comparison (based upon financial information as at 31 March 2018) indicates that the average general reserve balance (of the councils within the comparison group) is £3.871m and average earmarked reserves are £14.147m. By comparison, Somerset West and Taunton is predicted to have an opening general reserve balance of £2.828m but will have significantly higher earmarked reserves in excess of £25m.

7. CONCLUSION AND NEXT STEPS

- 7.1 The risk assessment and Audit Commission questionnaire are useful tools in establishing Somerset West and Taunton's minimum level of general reserves. This must be caveated with the assertion that if the Council relies on reserves to address a budget gap, and in particular for ongoing costs it will be immediately exposed to a heightened risk if it does not remain above the minimum level.
- 7.2 **With reference to the analysis that has been undertaken and with attention to the risks that the Council faces, a recommendation is made to set the minimum level of general reserves at £2.4m.**