GENERAL & EARMARKED RESERVES FRM(22)16.07

Recommendations

1. MPC, as part of its annual budgeting process, should review its General Reserve and the levels and purposes of all Earmarked Reserves, taking into account JPAG guidance.
2. MPC should consider setting up an earmarked reserve for "Budget Risk", on the basis suggested in the final paragraph in this note.

Guidance on Reserves

The Joint Panel on Accountability & Guidance (JPAG) 2021 guidance on reserves is attached to this note.

Melton's Position relative to the JPAG guidance on General Reserves

By comparison with Parish & Town Councils nationally, MPC should be categorised by size as "upper-small" or "lower-middle". Using the JPAG formula, this would produce a minimum general reserve for MPC equivalent to, say, 9 months Net Revenue Expenditure (NRE = Precept less Loan Repayment).

The base NRE for MPC, using 2022/23 figures, is £85k - the 9-month equivalent of which is £64k, excluding MPC's planned deficit for 2022/23 of £13k.

If MPC was aligned exactly to the JPAG guidance, it would start 2022/23 with a minimum level General Reserve of £64k. The latest forecast of MPC's general reserve at 1 April 2022 is £66k (it was £64k at 1 April 2021).

Melton's Position relative to JPAG guidance on Earmarked Reserves

MPC's earmarked reserves are used mainly as a repository for CIL money.

In 2019, our internal auditor recommended that MPC should set up an earmarked reserve to cover **Budget Risk**. For MPC, the main budget risks are the tenancy income and the cost of employing temporary cover in the event that a member of staff is off work for an extended period.

In response to the 2019 audit recommendation, MPC decided to continue using a single general reserve to cover all contingencies. In part, that was because MPC's general reserve was reduced (and reducing) and splitting some of it off to an earmarked reserve would have made matters worse.

There is, nevertheless, a principled, case for diverting some of the General Reserve into a “Budget Risk” Earmarked Reserve”. And there is more budget risk now than there was when MPC declined the internal auditor’s recommendation. The creation of a “Budget Risk” Earmarked Reserve would represent a tangible amelioration of the “financial risk” item in MPC’s Risk Register. It would also avoid our General Reserve appearing over-stated.

If MPC were to have a “Budget Risk” Earmarked Reserve it should agree an upper limit equivalent to, say 12 months rental income and 3 months of the gross pay budget (currently about £32k). It would not be prudent for MPC to transfer this whole amount in one go from General Reserve to the “Budget Risk” reserve.

The proposal is for the Budget Risk reserve to be built up over time:

- **starting with a £5k transfer in 2021/22. This would reduce the General Reserve to £61k at 1 April 2022, a level consistent with JPAG guidance;**

- **and a further £5k transfer in 2022/23;**

- **and for reserves to be subject to regular review, with future transfers to the Budget Risk reserve being made on a planned or opportunistic basis.**

Cllr. Bill Banks

Chair of FERM

8th April 2022

EXTRACT on "RESERVES" from Joint Panel on Accountability and Governance (JPAG) 2021

Annual Governance Statement Assertion

Reserves — The authority needs to have regard to the need to put in place a General Reserve Policy and have reviewed the level and purpose of all Earmarked Reserves.

***Reserves**:*

5.31. As with any financial entity, it is essential that authorities have sufficient Reserves (General and Earmarked) to finance both its day-to-day operations and future plans. It is important, however, given that its funds are generated from taxation/public levies, that such reserves are not excessive.

5.32. General Reserve — The generally accepted recommendation with regard to the appropriate minimum level of a Smaller Authority's General Reserve is that this should be maintained at between three (3) and twelve (12) months Net Revenue Expenditure (NRE). NRE (subject to any planned surplus or deficit) is effectively Precept\Levy less any Loan Repayment and/or amounts included in Precept\Levy for Capital Projects and transfers to Earmarked Reserves. The reason for the wide range (3 to 12 months) is to cater for the large variation in sizes of individual authorities. The smaller the authority the closer the figure should be to 12 months NRE, the larger the authority the nearer to 3 months. In practice, any authority with an NRE in excess of £200,000 should plan on 3 months equivalent General Reserve. In all of this it is important that each authority adopt, as a General Reserve policy, the level appropriate to their size and situation and plan their Budget so as to ensure that the adopted level is maintained. Changes in activity levels/range of services provided will inevitably lead to changes in the requisite minimum level of General Reserve in order to provide working capital for those activities.

5.33. Earmarked and Other Reserves — None of the above in any way affects the level of Earmarked and/or Capital Receipts Reserves (EMR/CRRs) that an authority may or should hold. There is, in practice, no upper or lower limit to EMR/CRRs save only that they must be held for genuine and intended purposes, and their level should be subject to regular review and justification (at least annually), and should be separately identified and enumerated. Significant levels of EMRs in particular may give rise to enquiries from Internal and/or External Auditors.