

Item: 5

Policy and Resources Committee: 19 December 2022.

Strategic Reserve Fund – Contribution to General Fund Services.

Proposed Notional Allocations.

Report by Head of Finance.

1. Purpose of Report

To consider allocating the contribution from the Strategic Reserve Fund to specific activities and areas within General Fund Services.

2. Recommendations

The Committee is invited to note:

2.1.

That, for many years, the Strategic Reserve Fund allocation to the General Fund has been used as one of the funding sources for all General Fund services rather than making a direct financial contribution towards specific service functions or items of expenditure.

2.2.

That the Strategic Reserve Fund contribution is attached to specific areas of General Fund expenditure in order that the Orkney public can see more readily the benefit of the Strategic Reserve Fund and the additionality of service provision that it allows the Council to deliver.

2.3.

That, although accounting for the contribution from the Strategic Reserve Fund as a direct contribution to specific services would have negative future consequences on expenditure-based budget distributions, notional allocations would avoid those negative consequences.

2.4.

The current performance of the Strategic Reserve Fund investment portfolio, as detailed in section 9 of this report.

It is recommended:

2.5.

That the Strategic Reserve Fund allocation to General Fund services for financial year 2023/24, amounting to £6,350,000, be notionally allocated as a direct funding contribution towards the service functions set out at section 5.2 of this report.

2.6.

That, should a higher contribution than £6,350,000 be required from the Strategic Reserve Fund to balance the General Fund budget for financial year 2023/24, this be treated as a source of funding for General Fund services and notionally allocated to Loan Charges.

3. Introduction

3.1.

The contribution from the Strategic Reserve Fund to General Fund services for 2022/23 amounted to £8,263,000, being the balance of the cumulative 3-year total of £22,050,000 recommended by the Policy and Resources Committee on 25 February 2020.

3.2.

On 21 December 2021, when reviewing the level of disbursements from the Strategic Reserve Fund used to support General Fund Services and other Council priorities for financial year 2022/23 onwards, the Policy and Resources Committee recommended indicative disbursements for 2023/24 and 2024/25 of £6,350,000.

3.3.

This level was based on the Investment Strategy Review carried out by Hymans Robertson and reported to the Investments Sub-committee on 27 May 2021, which stated:

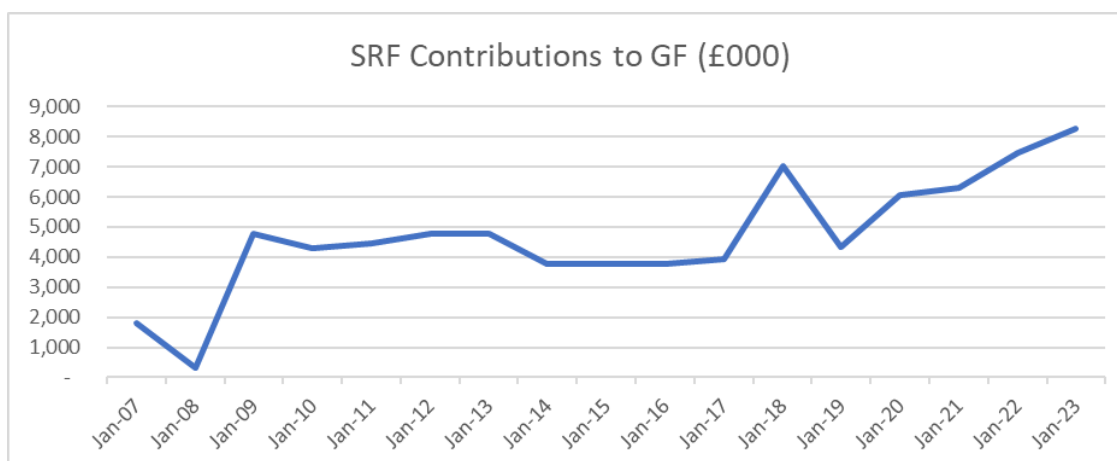
- The current expected return (from our models) of ~.5.2% per annum (nominal) can support distributions of £6.35m per annum whilst retaining the fund size over the long term, albeit it would take around 9 years for the Strategic Reserve Fund to return and exceed the current size given the higher planned level of distributions and expenditure in the short-term.
- Actual return needs to be at least 5% per annum to maintain the fund size with distributions of £6.35m per annum.
- The Fund should be expected to continue to support distributions of £6.35m per annum following a sudden fall in the fund asset base of ~ 3.0%, based on the current expected return, although it would take a long time, well in excess of 10 years, for the value of the fund to return above current levels.

3.4.

The Council faces significant real terms reductions in Government funding. In addition, Government austerity measures over many years, service pressures and increasing demand for services has meant the Council has faced significant budget savings measures. To mitigate the impact of these pressures the Council has elected to draw down Strategic Reserve Fund funding in order to protect local services.

3.5.

The following graph demonstrates the level of the funding gap over the years.



3.6.

The Council has been able to use the Strategic Reserve Fund for a great number of different applications over many years that fall within the broad terms of being for the benefit of the inhabitants of Orkney. The following table summarises the use of the reserve fund since 2000:

Summary	Total since 2000 £000
Capital Contributions	13,100
Community Development Fund (CDF)	1,422
General Fund Contributions	79,819
New CDF Scheme	2,000
Scapa Flow Oil Port (Surplus)/Deficits	19,106
Scapa Flow Landscape Partnership	229
Stromness Townscape Heritage Initiative	638
Housing Revenue Account Contribution	4,648

Summary	Total since 2000 £000
Island Games	55
North Isles Landscape Partnership	246
Strategic Projects – Renewables	2,255
Covid-19 Fund	3,000
Grand total	126,518

4. Background

4.1.

Historically the Strategic Reserve Fund had been applied largely for Economic Development purposes with expenditure charged directly to the Strategic Reserve Fund.

4.2.

The direct charging of expenditure to the Strategic Reserve Fund was not particularly transparent with some duplication of process and different reporting arrangements.

4.3.

With pressure on General Fund budgets, there was a change in practice from 2002/03, as part of a medium-term strategy, to support the case for additional support from the Scottish Government, with a direct contribution from the Strategic Reserve Fund to specific General Fund service areas, together with consolidation of budgets and spending. This contribution from Reserves enabled the Council to move from a budget overspend position to an underspend.

4.4.

This practice persisted for a few years until a change in accounting requirements led to the Strategic Reserve Fund contribution being applied as a source of funds for the overall budget rather than directly attributed to a specific budget area.

4.5.

The Council held five public engagement exercises over the summer of 2018 where there were several comments that the Council should start to use the Strategic Reserve Fund rather than “keep it for a rainy day”.

4.5.1.

These sessions demonstrated that there was a general lack of awareness that the Council has been using, and does use, the Strategic Reserve Fund, and there was some surprise from those attending the engagement events at the level of support from the Strategic Reserve Fund to both capital projects and General Fund services in recent years.

4.5.2.

The Strategic Reserve Fund contribution to General Fund services has enabled the Council to continue to provide many of the non-statutory services that add much to both the quality of life and cultural heritage of Orkney that have been subjected to significant budget cuts in many Council areas.

4.6.

The lack of awareness by the Orkney public of the benefit that the Strategic Reserve Fund affords in the delivery of services has led to elected members reflecting that the message on spend from the Strategic Reserve Fund could be improved if the spend was more readily identifiable and attached to service budget areas, particularly to those service areas that are very much discretionary but add significantly to the sense of community or cultural heritage of Orkney.

5. Proposed Notional Allocations

5.1.

Accounting for the contribution from the Strategic Reserve Fund as a direct contribution to specific services will have negative future consequences on grant aided expenditure assessments where the reserve contribution would count as income and result in reduced government support for those services in future. This would not however prevent the Council from notionally attaching the Strategic Reserve Fund contribution to General Fund budget areas.

5.2.

The table below sets out a proposed list of notional budget allocations, totalling £6,350,000, that largely consists of discretionary service areas that fit with the theme of benefiting the quality of life, health and wellbeing, and cultural heritage of Orkney.

	2022/23		2023/24	
	Notional Amount	Total	Amount	Total
Service	£000	£000	£000	£000
Chief Executive:				
Twinning	15		-	
Loan charges	1,328		28	
Third Sector Funding	142		142	
		1,485		170
Orkney Health and Care:				
Social Care Services	1,044		574	
Voluntary Services	785		785	
Small Repair grants	50		50	
Childcare Partnership/Family Support	59		59	
		1,938		1,468
Education, Leisure and Housing:				
Swimming pools	208		213	
Pickaquoy Centre	911		913	
Healthy Living Centres	96		76	
Outdoor Education service	83		86	
Active Schools	95		36	
Community Centres	296		267	
Youth Café	18		18	
Museums	293		268	
Library service	967		993	
Culture Fund	179		177	
St Magnus Cathedral	183		173	
Grounds maintenance	266		269	
Parks and play areas	80		81	
Music provision	30		-	
		3,705		3,570
Development and Infrastructure:				
Public Conveniences	85		90	
Economic Development grants	439		439	
Fairs, galas and community events	43		44	
Public Bus Contract	500		500	
Access to the Countryside	68		69	
		1,135		1,142
Total		8,263		6,350

5.3.

The changes relate to matching the 2022/23 budget except for the following:

- £15,000 against Twinning – this budget already sees this income amount as a source of funding, so this is removing this duplication.
- £1,300,000 in loan charges – this has historically been the balancing figure.
- £470,000 against Social Care Services – the Council should not be funding core services from its reserves, and funding will be met from within the settlement.
- £20,000 against Museums – reflecting the donation income anticipated from the new machines installed.
- £20,000 against St Magnus Cathedral – reflecting the donation income anticipated from the new machines installed.
- £30,000 against Music provision – this is now met from Scottish Government funding.

6. Implication for Budget Savings

6.1.

The implication for future budget savings exercises of notionally allocating the Strategic Reserve Fund contribution to specific General Fund service areas is that the contribution will be matched to those areas which are likely to be non-statutory, discretionary areas of spend and would accordingly have been the natural choice of proposed savings as the Council continues to face significant budget constraints. The consequence of this will be that Services will have greatly reduced choices from which to make any savings if discretionary areas of spend are effectively protected from cuts through the local funding of those services even if this is only notionally.

6.2.

The notional allocations have been set at 2022/23 budget levels. The saving opportunity for services is therefore limited.

7. Links to Council Plan

The proposals in this report support and contribute to improved outcomes for communities as outlined in the Council Plan strategic priority themes of Thriving Communities and Quality of Life.

8. Links to Local Outcomes Improvement Plan

The proposals in this report support and contribute to improved outcomes for communities as outlined in the Local Outcomes Improvement Plan priorities of Connectivity and Community Wellbeing.

9. Financial Implications

9.1.

The contribution from the Strategic Reserve Fund recommended to be notionally allocated against areas of General Fund spend has been set at £6,350,000.

9.2.

Should the Strategic Reserve Fund contribution required to balance the General Fund budget be greater than £6,350,000, any additional contribution would be used as a source of funding and notionally allocated to Loans Charges.

9.3.

The Strategic Reserve Fund Investment Strategy Review, carried out by Hymans Robertson and referred to at section 3.2 above, highlights the risk of

- Making higher than affordable allocations from the Strategic Reserve Fund.
- The impact on the fund of poor investment returns.

9.3.1.

In 2022/23 the allocation was £8,263,000, which is £1,913,000 above the £6,350,000 allocation considered by the Hymans Robertson report. The Strategic Reserve Fund return on invested funds to 30 September 2022 was -8.8%, below the -3% 'shock' considered by the report.

9.4.

Current projections show that the current long-term calculations based on 2022/23 activity will take 10 years for the 'floor' to rise back above real terms value of fund, set in April 2012, subject to the performance of the market, and the Council's Strategic Reserve Fund equity portfolios.

10. Legal Aspects

10.1.

Section 95 of the Local Government (Scotland) Act 1973, as amended, obliges the Council to make arrangements for the proper administration of its financial affairs.

10.2.

Section 69 (3)(e) of the Orkney County Council Act 1974 permits the Council to apply any reserves established thereunder for any purpose which in the opinion of the Council is solely in the interests of the County or its inhabitants.

10.3.

The Council must make arrangements which secure best value. An authority securing best value will be able to show that it is making effective and efficient use of its financial resources.

11. Contact Officer

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