Association of Mental Health Providers

RESERVED

THE IMPORTANCE OF FINANCIAL RESERVES IN BUILDING RESILIENCE IN MENTAL HEALTH CHARITIES

FINANCIALRESERVES IN MENTAL HEALTH CHARITIES

Association of Mental Health Providers is the national voice of mental health charities providing services in England and Wales, representing the full spectrum and diversity of third sector service provision. Within our alliance, we have over 300 members delivering over 3000 services locally, regionally, and nationally, with a significant reach of over 8 million people affected by poor mental health and illness.

In recent years the combination of the COVID-19 pandemic and rising operational costs have significantly impacted mental health charities, leading to a sharp increase in demand for their services while simultaneously causing a decline in overall income.

This briefing paper explores the current state of charity reserves in light of these developments, highlighting the financial pressures and the need for strategic planning to ensure sustainability in the face of ongoing uncertainty.

64% of the Association of Mental Health Providers' members indicated in May 24 that they had seen erosion of their reserves over the last 5 years to a point that would lead to financial instability if there was a further need to cross-subsidise public services for another 12 months.

In light of increasing concerns expressed by members about their organisation's financial reserves and the expectations and assumptions made by some public funders and commissioners about the use of these, the Association has developed the following position statement that it hopes will guide national and local approaches to supporting the sustainability of the sector.

This work has been led by Jane Hughes and Sarah Maguire, CEOs of Mental Health Matters and Choice Support respectively, and Trustees of the Association of Mental Health Providers

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Key points:

- A robust reserves policy not only assures internal and external stakeholders of responsible financial stewardship, but also safeguards an organisation against unforeseen challenges. The policy should consider the size, risks, and income streams of the organisation.

- Charity Commission guidance encourages linking reserves policy to risk management, budgets, and spending plans. VCSE are advised to develop simple plans and budgets. In June 2023, the Charity Commission issued the latest update to its guidance on reserves (CC19 – Charity Reserves: Building Resilience).

- We also recommending looking beyond the traditional definitions of reserves and considering wider parameters like cash and liquid reserves to gain a holistic view of their financial flexibility.

- Within mental health VCSE services our members concerns are that reserves after adjustments are being significantly impacted by statutory contract underfunding. In practice this means the amount of reserves held at the end of the reporting period after making allowances for any restricted funds, designations, commitments, or the amount of functional assets representing a commitment of reserves are diminishing significantly. This is putting pressure on the stated free reserves of many members.

- Subsequently, setting a target level of reserves is becoming increasingly difficult. Organisations should consider factors like the predictability of their income, future planned expenditure, and identified financial risks.

- Among the top 100 UK charities, over a quarter do not disclose a specific reserves target, and about one-third opt for a target range rather than a singular figure to provide more flexibility.

- While most our members have seen consistent year-on-year decreases in actual reserves, fewer have increased their reserves targets, raising questions about their strategic approach to financial risk.

A model reserves approach for VCSE providers

The size of any reserve is based on a number of factors that differ by organisation. For example, you can develop a reserve policy that specifices maintaining a minimum of 6 months indirect costs.

There is also a need to hold funds back for services in deficit, investment in tech and infrastructure. The amount or percentage of the total organisational turnover may be variable therefore; a set of guidelines might be more appropriate.

For example:

- 6 months of all indirect costs (overheads)
- An amount for investment / re-investment in tech and infrastructure, near and longer term needs (amount to be driven by strategic objectives of the business)
- An amount to cover services that are currently in deficit for a short term, (based on historical trends and business targets for improvement)

Year on year organisations should aim to ensure that all contracts fully cover costs of delivery a small deficit.
This, however, is very challenging to achieve in our sector and inevitably as care providers will always have some contracts that are not fully covering costs of delivery. In the short term reserves should be set at a level that affords the organisation time to renegotiate /transform these contracts.

However, this should be for a limited time period not exceeding 1 financial year, depending on the size of contract. Persistent deficits due to underfunding are detrimental to financial resilience as they very quickly deplete cash reserves and general reserves.

In summary, we are highlighting the importance of well-designed reserves policies in ensuring VCSE MH financial resilience, and the evolving practices required by statutory funders to limit financial instability of essential services in mental health social care.

Read our paper *"Developing positive engagement between commissioners and the VCSE provider sector,"* which outlines a number of issues to be considered by commissioners and providers to support long term effectiveness of the sector within the health and care system.