Leeds City Council

Review of the Financial Plan

12 October 2005

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Contents

1 Executive Summary

1.1 Introduction

The medium term Financial Plan is the key financial document that underpins the strategic direction of an organisation. The Council has recently published its third Financial Plan, the purpose of which is to support the Council's corporate planning processes, and to indicate the resource issues and principles which will shape the Council's financial strategy and annual budgets. We have reviewed the processes surrounding the Financial Plan and have undertaken a "healthcheck" to ensure it recognises national and local risks. We have also considered the process of funding Corporate Plan priority areas.

1.2 Key Findings

The Council's Financial Plan reflects the national and local issues that the Council faces and also reflects the strategic direction set out in the new Corporate Plan although it was published prior to the Corporate Plan publication. This timing issue is the main issue the Council face in their service and financial planning. The Council has already recognised the adverse impact of this on its service and financial planning arrangements and the need to reinforce the links between service planning and budget

The formal arrangements to monitor and review the Council's Financial Plan are also limited. Currently these only include a high level review during the annual budget process and an annual report to members. Other Council's and good practice suggests that arrangements should include formal on-going review to ensure the Financial Plan remains relevant in the context of new and emerging issues and the success of the Financial Plan is measured through a system of targets and milestones which are regularly reviewed. The core of this approach is an ongoing approach to the identification and management of corporate level risk.

The Council has already taken steps to develop its approach to identifying priority and lower priority areas both in a CPA context and because this will reinforce the Council's ability to move resources from lower priority areas to more priority areas. Further to this, the Council has also taken steps to establish a corporate framework and governance arrangements for Gershon efficiency savings although progress in Departments appears to be mixed, with some Departments making arrangements for identifying future savings and with others waiting for centrally organised initiatives.

The Council's reserves policy establishes a requirement for Departments to prepare budget action plans for variations against departmentally controlled budgets of up to 2% of net expenditure and the need to increase reserves to a range of £14m to £18m by 2007/2008. However, the reserves policy does not directly consider the Council's medium term corporate risk profile. The introduction of the budget risk process and further development of risk management, through the Risk Management Framework means that the Council are in a position to develop a more risk based approach to setting the level of reserves.

In the last two financial years and in the current financial year the Council has allocated significant amounts of money to Corporate Plan priorities. However, the Council and Departments have not consistently evaluated the impact of the additional funding in terms of service outcomes for users. Therefore, the Council has been unable to fully measure the success of the different allocations of money to Corporate Plan priorities. Good practice suggests that when additional funding changes are made reflecting Corporate Plan priorities, the Department receiving the additional funding should be asked to demonstrate and measure how the funding will improve service outcomes for users. Looking forward to CPA 2005, evidence of resources following priorities and subsequent changes in service volume and quality will be important.

1.3 Key Learning Points

- The Financial Plan should be monitored to ensure it remains relevant and reviewed against a series of targets/milestones designed to measure whether the high level objectives of the plan are being met.

- In line with current intentions the service and financial planning timetable needs to be integrated to allow the corporate and financial plans to inform service and budget planning in the annual cycle. This timescale requires consideration of corporate risk for the following year very early in the annual cycle.

- The Council need to develop an explicit corporate risk register as a matter of urgency and then an assessment of the relationship between risk and reserve levels with the aim of developing a risk based reserves strategy for adoption by the Council in its 2006/7 budget.

- The Council need to ensure when additional funding is provided for Corporate Plan priorities, the Department receiving the additional funding is required to demonstrate and measure how the funding will improve service outcomes for users. This then needs to be monitored to show the success of the additional funding in the priority areas.

1.4 Way forward

We will discuss the findings of the review with officers to agree an action plan to address the key issues going forward. In addition, we shall continue to work with officers to constructively challenge the delivery of action plans.

2 Introduction

2.1 Background

Financial management is a key element of a Council's overall management arrangements. In May 2004, CIPFA introduced its new model of financial management which included the following definition:

"Financial management is the system by which the financial aspects of a public body's business are directed and controlled to support the delivery of the organisation's goals."

The Financial Plan is an instrumental document in this process and should assist the Council in determining policy and financial choices.

2.2 Objectives and scope of the review

The scope of our audit is to:

- undertake a health check of the Financial Plan to ensure it reflects; the strategic direction of the Council; the key national issues and initiatives; and new corporate projects and issues in the Council's medium-term horizon (Section 3);
- review the process for developing, maintaining and monitoring the Financial Plan to ensure that all parts are coherent including; integration with the Council's risk management arrangements; corporate capacity for achieving the Financial Plan; and arrangements for linking service and financial planning (Section 3 and 4);
- review the extent to which the Financial Plan and risk based reserves strategy are integrated (Section 4);
- review the degree to which the allocation of additional resources provided in the past have resulted in service improvements (Section 5);

- map investment in priority areas to outcomes/quality of improvement in services (Section 5);
- ensure the implications of the Prudential Code are reflected in the Financial Plan (Section 6);
- ensure the Financial Plan is consistent with the Council's capital programme (Section 6); and
- highlight links between use of resources and financial planning to support preparations for CPA 2005 (Throughout).

2.3 Audit approach

Our approach has been to:

- review key documents such as the Financial Plan, Capital Programmes and Council Plan;
- review selected service plans;
- interview key officers, including the Chief Officer for Financial Management and Heads of Finance for various different Departments; and
- apply various audit tools assessing specific issues.

2.4 Social Service budget position

The Social Service budget position is one of the significant financial issues facing the Council, however this review has not considered this issue because it has been considered as part of a separate review and a separate report has been issued.

2.5 Acknowledgements

We would like to take this opportunity to thank all those staff at the Council who have supported this review.

3 The Financial Plan

3.1 Introduction

This section reviews the Financial Plan to ensure that it reflects developments in the Council's strategic and service planning framework and associated corporate projects and issues in the Council's medium-term horizon. The section also considers the plans for developing, maintaining and monitoring the Financial Plan.

3.2 Background

The Council's Financial Plan was published in November 2004 and sets out:

- the context within which the Financial Plan was prepared;
- the principles underlying the development of the plan;
- the projected revenue and capital plans for 2005/08; and
- support for the delivery of the Council's key priorities.

3.3 Strategic direction

There is an established process to ensure that the Council plan reflects the Council's priorities. Our review confirms that the Financial Plan takes account and reflects; the strategic direction within the Council's Corporate Plan; key national issues and initiatives; and projects within the Council's medium-term horizon. As the plan was completed prior to the current corporate plan there are some inconsistencies in terminology. More importantly there is a need to align the timescales in updating Service plans and the Financial Plan with the annual budget cycle. We understand that this will be addressed as part of other planned changes to the service planning and service performance management framework. This link will make it easier to provide a transparent link between corporate priorities and both annual and medium term financial investment to support their achievement.

Recommendation 1

The Council should amend the corporate and service planning framework to ensure that updates to the Financial plan inform the annual service and budget planning process.

3.4 Key national and local issues

The Financial Plan reflects the significant national and local issues faced by the Council, these issues include:

- Gershon efficiency savings. The Council's progress and arrangements are discussed in Section 3.7.
- Significant issues, where the government has issued consultation papers and proposals on, such as:

  - Local Government Funding Inquiry;
  - Business Improvement Districts;
  - Local Authority Business Growth Incentives; and
  - Council Tax revaluations.

- Private Finance Initiative (PFI). The Financial Plan mentions existing and possible future uses as well as existing financial issues with PFI.

- The Children's Bill. The Financial Plan mentions the key features of the Children's Bill and the fact that there will be resource implications in the future.

- Single Status, equal pay claims and the pay review. The Financial Plan mentions the key issues and recognises that these issues potentially carry significant costs for the Council.

3.5 Monitoring and review of the Financial Plan

Officers have identified that the Annual Budget Report and process, and an annual report to members is the method by which the plan will be reviewed. However, these are separate activities that do not represent a formal regular review of the Financial Plan.

To undertake this review/monitoring of their Medium Term Financial Strategies, other Councils have developed Financial Strategy Groups with membership from senior management and senior finance officers with a formal terms of reference which include significant areas such as:

- financial overview of major projects;

- financial planning and risk analysis;

- new and emerging issues; and

- success of the Financial Plan.

The Council has also recently introduced a corporate risk management group who will consider the impact of corporate level risks including their financial consequences. The outcomes from this group will enable significant financial issues to be more formally tracked in relation to the medium term financial plan.

The Financial Plan does not currently identify any criteria to measure its success. The Council should develop a series of targets/milestones that demonstrate the success the Council has had with implementing the Financial Plan.

Recommendation 2

The Council needs to identify and implement a formal mechanism to review the Financial Plan on a regular basis, including a series of targets/milestones to measure the success of implementing the Financial Plan.

3.6 Service and financial planning

The linkages between service and financial planning are essential to deliver the service priorities that the Council desires. Also the Audit Commission's key lines of enquiry for use of resources specify the importance of integrating business and financial planning. The Council already accept weaknesses exist in this area and have started to develop a new business planning model as set out above. Our review of the existing arrangements found that all the Departments reflected the service priorities that had been identified in financial planning/budget processes but these service priorities were not necessarily the complete or the final priorities. Further to this the formal links between service priorities and budgets were difficult to identify.

Good practice suggests that service planning in accordance with the corporate strategy documents should identify key service priorities that should then be considered financially and then incorporated in the budget where possible. This will improve the links between service planning and the budget. The good practice also suggests that service and financial planning should be considered prior to the traditional budget preparation cycle beginning. The planned developments set out in Section 3.3 above should take the Council some way towards achieving this recommendation.

Recommendation 3

The Council should establish a service and financial planning framework that allows service priorities key to the Council's corporate priorities to be identified and considered as part of the budget preparation cycle. This can be completed by starting the service planning cycle earlier, to enable all priorities to be identified and then considered as part of the budget cycle**.**

3.7 The Council's priorities

The Council's 2005 CPA report stated that there is a lack of clarity about what are not priorities and this means movement of resources from lower priority services remains limited. The Council has developed a framework for assessing the financial consequences of the Council's priorities in the budget process and it is planned that this will be supplemented to assist the consideration of savings and reinvestment options. We also note that the Development Department used this as a guide to help in formulating budget decisions. Although this initial exercise did not provide a final outcome in terms of identifying lower priority services, the Council needs to continue to develop this further and implement such a model to be able to meet the challenges of budget pressures over the foreseeable future and therefore use resources appropriately.

Recommendation 4

The Council's approach that is currently in development needs to integrate consideration of the annual efficiency statement with a mechanism to demonstrate how resources follow priorities as part of the annual budget process and in the medium term context of the financial plan.

3.8 Gershon efficiency achievement

One of the important features of service and financial planning over future years is going to be Gershon efficiency savings. Whilst the Departments have identified efficiency savings, many of these have stemmed from planned savings the Council needed to make to balance the budget and it is not transparent the extent to which ongoing savings will be consistent with the Council's priorities in the medium term. Review of the Departments' plans for future developments for Gershon savings has been mixed, whilst some Departments have put in place arrangements to start developing areas for future savings, others have not and appear to be waiting for Council initiatives before taking the next steps.

It is encouraging to note the Council has identified a corporate framework and governance arrangements for the Gershon efficiency savings agenda and are incorporating links to service transformation. This should help Departments reflect the importance of the exercise and not treat it as a year end exercise to complete the Annual Efficiency Statement.

Recommendation 5

The Council needs to ensure the development of Gershon efficiency savings is implemented in all Departments as early as possible to ensure all possible areas of savings are reviewed.

4 Risks Based Reserves Strategy and Risk Management

4.1 Introduction

This section considers the extent to which the Financial Plan and risk based reserves strategy are integrated, including how well risk management arrangements are integrated into financial planning.

4.2 Background

The Council has now formally set out its reserves policy. The key features of this are:

- arrangements for departmental management of budgetary risk;
- £3m contribution to reserves in 2005/2006; and
- increase in reserves to a range of £14m to £18m by 2007/08.

4.3 Reserves Policy

The Council has introduced a policy that requires the Departments to prepare budget action plans which sets out how they will deal with spending variations on departmentally controlled budgets during the year, up to a limit of 2% of net expenditure.

The 2005/06 budget proposes that reserves are increased to £12.0m, which requires a £3.0m contribution into reserves. The policy also states it is reasonable to set a range of 3% and 4% of net expenditure (excluding schools) for the level of reserves by 2007/08, this equates to a range of £14m to £18m.

The Council also has a number of well developed specific processes for considering areas of risk for example in relation to PFI and other major projects.

The current reserves policy does not explicitly consider the financial consequences of known corporate risks in determining the level of reserves that are required. The recent introduction of a corporate risk management group provides the opportunity to ensure that the financial consequences of the corporate risk register are considered in the context of the general risk based reserve policy. This should also be linked to the Council's prudential borrowing and the relationship to specific provisions and reserves where risk exposure could exceed amounts specifically set aside. To be explicitly risk based and to meet the new criteria for CPA 2005 the policy needs to be more specific about the relationships between risk and reserve levels as a function of both value of the risk and proximity of the risk event.

The Council is already considering how to develop its approach to longer term risks as part of the development of its risk management arrangements.

4.4 Risk Management

Risk management is the process by which threats and opportunities on an organisation's objectives are identified, evaluated and treated. The Council has recently published its Risk Management Framework, which aims to make risk management an integral part of existing business functions and service planning. Currently the Council does not have a corporate risk register, which captures all non-financial and financial risks. Therefore, it is understandable at this stage that the Council can not entirely rely on a risk based reserves strategy, to determine the level of reserves.

Recommendation 6

The Council need to implement their Risk Management Framework, and then develop a more risk based reserve policy which is specific about the relationship between risk and reserves level.

4.5 Budget risks

The Council has developed a risk based approach to budget monitoring through the introduction of a budget risks register process by which budget risks are identified and rated using a risk matrix, this matrix is shown in the table below.

Table 1: Budget Risk Matrix

	Probability		**Impact**
Score	**Description**	**Score**	**Description**
1	Rare	1	Insignificant (£0 - £499k)
2	Unlikely	2	Minor (£500k - £999k)
3	Possible	3	Moderate (£1,000k - £1,499k)
4	Probable	4	Major (£1,500k - £1,999k)
5	Almost certain	5	Highly significant (Over £2,000k)

The scores from each category (Probability and Impact) are multiplied to produce a total score, which determines the risk classification as high, medium or low. For these risks the Council has produced a corporate budget risk register, which aims to identify the budget risks. This budget risks process is formally reported on a quarterly basis, although the risk management process for these risks in the Departments is an ongoing process.

Our review of the budget risk registers and the process identified the following:

- whilst some Departments were clearly able to identify why specific risks had been rated and scored as they were, other Departments were unable to provide this evidence;
- all risks reviewed showed evidence of management action as stated in the risk registers;
- all risks had a risk owner; and
- not all risks were accurately updated on a quarterly basis, for instance one risk which had significantly reduced from quarter 1 to quarter 3, had an inappropriate impact score in quarter 3.

The underlying process should provide a sound basis for the Council to develop a more risk based approach to setting the level of reserves, after the establishment and management of a corporate risk register.

Recommendation 7

The Council should ensure the budget risk process accurately reflects the budget risks the Council faces and that all risks are accurately updated. The Council also needs to consider the explicit top down integration of corporate risk.

5 The Financial Plan and service improvements

5.1 Introduction

This section considers the degree to which the allocation of additional resources provided in the past have resulted in service improvements and maps investment in priority areas to measurement of outcomes / quality of improvement in services.

5.2 Background

Additional resources are usually directed to priority areas to tackle priority issues (as identified by the Corporate Plan). The table below shows the current Financial Plan priorities and previous Medium Term Financial Plan (MTFP) priorities.

Table 2: The Council's Priorities

Current Financial Plan Priorities		**Previous MTFP Priorities**	
Improved education attainment	Help vulnerable adults live independently	Creating better neighbourhoods and confident communities	Making the most of people
Housing decency standards	Extra funds for community safety across the city	Competing in a global economy	Integrated transport
Environmental safety	Improved customer services	Looking after the environment	Completing and implementing a fundamental organisation review
Regeneration		Improving leadership capabilities	Addressing equality issues
		Improving access to council services	

5.3 Additional resources for Corporate Plan priorities

For both sets of priorities the relevant annual budgets allocated additional resources for Corporate Plan priorities. The table below shows the additional funding that has been identified in the relevant annual budgets for Corporate Plan priorities.

Table 3: Additional funding for Corporate Plan Priorities

Year	Additional funding for Corporate Plan priorities (£000's)	Example of uses for additional monies
2003/2004	4,300	Development and enhancement of Anti-Social Behaviour Units Establishment of an environmental call centre Electronic booking of sports facilities
2004/2005	5,700	Further investment in initiatives above Further investment in CCTV Anti-graffiti drive through educational awareness
2005/2006	11,090	East and South East Leeds Regeneration Police Community Support Officers Purchase of additional library book Tackling anti-social behaviour in parks Funding for the initial revenue costs associated with procuring PFI Schemes (e.g. Street lighting)

Review of the previous MTFP's additional resource allocations to priority areas identified that resources were spent in accordance with the relevant priority area, but the Council corporately did not identify or monitor expected service improvements. Further to this, Departments that received the additional resources did not in all cases identify and measure the expected service outcomes from the additional resources. Good practice suggests that when additional funding is provided for Corporate Plan priorities, the Department receiving the additional funding should be asked to demonstrate and measure how the funding will improve service outcomes for users and that these success criteria are then used as part of the post implementation review .

One area that was measured related to Access to Services, which was allocated £500k in 2003/2004. Here the biggest elements of funding were used to develop an Environmental call centre; improve opening times and call performance in other call centres; and introduce electronic booking of sports facilities. The Department responsible, Corporate Services identified a series of performance indicators with targets and baselines to measure the success of the additional funding. An example of the targets is below:

- Percentage of customers satisfied they can contact the Council easily;
- Call answer rate; and
- Percentage of sports bookings carried out electronically.

Ongoing service monitoring of access to service targets has been integrated into ongoing monitoring of service effectiveness.

5.4 Current Financial Plan priorities

Review of the current Financial Plan's additional resource allocations to Corporate Plan priorities identified that the Departments have planned the nature of the expenditure, but have not in all cases identified how improvements in service outcomes will be measured. In addition to this, the Council has not requested Departments to identify the expected impact, in terms of service outcomes of the additional resources.

The Council needs to be able to measure the success of the additional resources for Corporate Plan priorities. This will become increasingly important as CPA becomes more focused on Councils' use of resources. The Audit Commission's key lines of enquiry for Use of Resources for Financial Management now specifies that councils should be able to demonstrate how financial plans and strategies have contributed to the achievement of corporate objectives.

Recommendation 8

Departments should identify the expected service outcomes in terms of targets and baseline information as part of the additional budget bid and then monitor the performance both during and after the investment is made in the priority area. Centrally the Council should monitor expected service improvements from the additional resources provided to Departments for Corporate Plan priorities.

5.5 Level of resources allocated to service priorities

The Council must ensure any resources that are allocated to a particular priority area are actually used on the priority area, and not used to fill budget gaps. This is important because otherwise the Council's priorities are not receiving the investment they need.

We undertook a review to identify if all resources identified as Corporate Plan priority resources were used in the stated priority areas. In all instances reviewed the resources were being used for the corporate plan priorities.

6 Capital

6.1 Introduction

This section considers the extent to which implications of the Prudential Code and Capital Programme are reflected in the Financial Plan.

6.2 Financial Plan's statement on Capital Plans 2004-2007

The Financial plan should provide a medium term context for both total capital commitments and the extent of ongoing revenue finance to the capital programme. It should not duplicate either the Council's capital programme, prudential borrowing strategy or asset management plan but should provide sufficient detail to demonstrate that priority projects can be funded and that capital enhancements to existing assets required to deliver corporate priorities can be delivered.

The Financial Plan includes a section on Capital Plans which identifies:

- £350m of capital investment highlighted in the Asset Management Plan that is not provided for;
- The Capital Expenditure in the Capital Programme 2004/2005 to 2006/2007;
- How the 2004/2005 Capital Programme is to be resourced; and
- Strategy for resource allocation.

The Financial Plan does not mention the Prudential Code, but does mention the Capital Strategy which discusses the Prudential Code.

The Financial Plan reflects the Capital Programme in the Capital Plan section. However, the detailed Departmental Plans in the Financial Plan do not reflect the level of capital expenditure intended to be funded from revenue or the major schemes which are planned/being procured, even though these are likely to have a significant impact on the Departments' approach to meeting Corporate Plan priorities.

Recommendation 9

The Financial Plan should identify the major schemes being planned/procured and their links to the Council's priorities.

Recommendation 10

Whilst the Financial Plan does explicitly consider the expenditure required to support asset management plans. The plan should also explicitly consider the funding options that asset disposals could give within the financial plan in the medium term.

Appendix 1

Recommendations and Action Plan

* * *	*Significant residual risk*	* *	*Some residual risk*	*	*Little residual risk*

	Recommendation	Priority	Management response	Responsibility and timescale
1	The Council should amend the corporate and service planning framework to ensure that updates to the Financial plan inform the annual service and budget planning process.	* *	Agreed. In line with the Government's Spending Review timetable, a new Financial Plan is produced every two years. In the interim year, the intention is to produce a review, and it is intended that this is submitted to the Executive Board in November 2005. For the future the review mechanism will be clarified within the Financial Plan.	Chief Officer – Financial Management. By November 2005
2	The Council needs to identify and implement a formal mechanism to review the Financial Plan on a regular basis, including a series of targets/milestones to measure the success of implementing the Financial Plan.	* * *	Agreed and as above.	Chief Officer – Financial Management. By Financial Plan 2006
3	The Council should establish a service and financial planning framework that allows service priorities key to the Council's corporate priorities to be identified and considered as part of the budget preparation cycle. This can be completed by starting the service planning cycle earlier, to enable all priorities to be identified and then considered as part of the budget cycle.	* * *	Agreed. The Council's priorities are clearly stated within its corporate plan, and these form the basis of decisions about resource allocation and realignment.	
4	The Council's approach that is currently in development needs to integrate consideration of the annual efficiency statement with a mechanism to demonstrate how resources follow priorities as part of the annual budget	* *	Agreed.	Chief Officer – Financial Management and Head of Performance and

	process and in the medium term context of the financial plan.			Improvement,
5	The Council needs to ensure the development of Gershon efficiency savings is implemented in all Departments as early as possible to ensure all possible areas of savings are reviewed.	* *	Agreed.	Corporate Efficiency Board
6	The Council need to implement their Risk Management Framework, and then develop a more risk based reserve policy which is specific about the relationship between risk and reserves level.	* * *	Agreed that there are areas of the risk based reserves policy which require further development, but professional judgement will continue to be an important element in determining the Council's risk based approach to reserves.	Chief Officer – Financial Management. Budget 2006/07
7	The Council should ensure the budget risk process accurately reflects the budget risks the Council faces and that all risks are accurately updated. The Council also needs to consider the explicit top down integration of corporate risk.	* *	Agreed. The identification and monitoring budget risks is as a process still being embedded.	Chief Officer – Financial Management. Further guidance on the matter has been provided to departments.
8	Departments should identify the expected service outcomes in terms of targets and baseline information as part of the additional budget bid and then monitor the performance both during and after the investment is made in the priority area. The Council should monitor expected service improvements from the additional resources provided to Departments for Corporate Plan priorities.	* * *	Agreed. Monitoring resource investment in terms of service improvement will be a key element of the Council's service prioritisation that is currently under development. Intention will be that it is incorporated within the Council's performance management framework.	Head of Performance and Improvement and Chief Officer – Financial Management. For 2006/07.
9	The Financial Plan should identify the major schemes being planned/procured and their links to the Council's priorities.	* *	To be considered further, although main vehicle for delivering capital investment is the Council's asset management plan and the capital	Chief Officer – Financial Development. Financial Plan

			programme.	November 2006
10	Whilst the Financial Plan does explicitly consider the expenditure required to support asset management plans. The plan should also explicitly consider the funding options that asset disposals could give within the financial plan in the medium term.	* *	Agreed. Much of this is encompassed within the Council's Asset management Plan, but could consider ways in which stronger links could be made between this and the Financial Plan.	Chief Officer – Financial Development This will normally be down within the Council's performance management framework.