

# **Strategic financial management in councils**

**Delivering services with a reduced income**

September 2010

**The Audit Commission is an independent watchdog, driving economy, efficiency and effectiveness in local public services to deliver better outcomes for everyone.**

**Our work across local government, health, housing, community safety and fire and rescue services means that we have a unique perspective. We promote value for money for taxpayers, auditing the £200 billion spent by 11,000 local public bodies.**

**As a force for improvement, we work in partnership to assess local public services and make practical recommendations for promoting a better quality of life for local people.**

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On Friday 13 August 2010, the DCLG announced that the Audit Commission will be abolished in 2012/13. This national report was completed before that announcement. The themes and messages of the report, including the self-help tools, remain relevant for councils in this time of economic uncertainty.

## Introduction

### The challenge ahead

**1** Councils face severe and long-term social and financial challenges. Demand for local services is growing. Demographic change, particularly an ageing population, places increased pressure on local services. The 2008/09 recession coincided with increased demand for school places and social care (Ref. 1).

**2** The financial pressures that councils face depend on the balance of different sources of income. District councils have already had to deal with reduced income from fees and charges (Ref. 1). Many councils' incomes from investments declined as interest rates fell. Reduced economic activity has cut income from planning fees, rents, car park charges, and capital receipts. Councils have in-year cuts in government grant for 2010/11 and the prospect of future reductions following the 2010 spending review. As well as general reductions, there will be focused challenges as central government ends particular funding streams.

**3** The government plans to eliminate the structural deficit by 2015/16. Public spending will have to fall. Councils will play a major part in helping to reduce the deficit. Cross-government cuts of £6.2 billion for 2010/11 were announced in June 2010 (Ref. 2). Local government's contribution in 2010/11 is £1.166 billion (Ref. 3).

**4** The emergency budget (Ref. 4) outlined the framework for the 2010 spending review. Spending on non-protected activities is likely to fall by an average of 25 per cent.

**'Ensuring that taxpayers' money is well spent is the fair and responsible way to reduce the deficit.'**

HM Treasury,  
*The Spending Review Framework, June 2010.*

**5** The October 2010 spending review (Ref. 5) will set the overall public spending levels for the period 2011/12 to 2014/15 – the expected life of the current Parliament. The spending review will clarify where cuts will be more, or less, than the 25 per cent average discussed in the budget. It will also say how cuts will profile over the four years of the spending review period.

**6** Councils face the challenge of planning to manage services as income from central government falls. Income from central government will fall. Councils will have few opportunities to raise income from fees and charges until the economy strengthens. And they will work in partnership with government to freeze council tax levels in 2011/12 (Ref. 4).

**7** The Audit Commission's use of resources assessments showed steady overall improvement in councils' scores between 2005 and 2008 (when the system changed). In 2005, 44 per cent of councils performed at or above minimum standards; by 2008 this had increased to 77 per cent (Ref. 6). Times have changed: councils face a markedly different future. Some councils have always taken a long-term view and they are well placed to respond proportionately. Others have focused on a closer horizon: they are likely to find it harder to adjust. The research for this paper shows a mixed picture of some excellent practice but much scope to improve.

**8** Councils that work to a longer time horizon will be in a stronger position to test the likely impact of different income scenarios, seek out alternative models for sharing local resources more effectively, and increase the impact of their spending and influence. They should review the relevance and the volume of services they provide and challenge the design, management, and delivery of services. Improving efficiency and streamlining processes, while necessary, will not be enough. There will have to be trade-offs between cutting to meet the current challenge and preserving capacity for the long term (Ref. 7).

**9** This paper will help council leaders, elected members, chief executives and finance directors to review how they will manage with less money. Councils can use this paper and the accompanying tools to understand where they can improve financial management and to begin to make those improvements. Councils can:

- test financial management approaches using the strategic financial management checklist and the list of common problems;
- use the illustrations of notable practice to learn from others; and
- take stock of how well prepared they are for the future by completing the value-for-money self-assessment.

# Austerity and opportunity

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**Councils must balance reduced income with increased demand for services. This chapter describes how good financial management will help councils to manage with less money.**

### Good financial management

**Good financial management is essential for the delivery of good public services and the effective stewardship of taxpayers' money.**

**10** Good financial management is essential for the delivery of good public services and the effective stewardship of taxpayers' money. It will help councils to make the right decisions for the short, medium and long term.

**11** The Audit Commission described the principles of good financial management in a discussion paper in 2005 (Ref. 8). Good financial management:

- is essential to good corporate governance;
- forms part of the firm foundations of an organisation as it underpins service quality and improvement;
- is the basis of accountability to stakeholders for the stewardship and use of resources;
- is about managing performance and achieving an organisation's strategic objectives, as much as managing money; and
- is a key management discipline, something that all non-executives and managers within an organisation are responsible for, individually and collectively.

**12** The five themes of good financial management link financial planning to decision making and service outcomes (Table 1).

### Managing the challenge

**13** Organisations that adopt the principles of good financial management can plan and manage for the long term. They are adaptable and financially resilient.

**14** In times of financial stability or income growth, short-term planning is an acceptable and often successful strategy. Paradoxically, it is during periods of turmoil and challenge that organisations need to manage for the longer term.

**Managing for the long term is not about predicting the future: it is about planning for it.**

**15** Managing for the long term is not about predicting the future: it is about preparing for it. Planning involves understanding future demand, assessing the impact of probable changes, and reviewing the gaps between funding needs and possible income. Councils can start to plan for the long term and make better use of their financial plans to:

- prepare for the unavoidable;
- pre-empt the undesirable; and
- control the controllable (Ref. 9).



Table 1: Five themes of good financial management

Theme	Description
Financial governance and leadership	Top management (both executive and non-executive) are financially literate. They understand the council’s financial environment. They foster an organisational culture that takes individual and collective responsibilities and accountability seriously.
Financial planning	There are links between the council’s strategic and corporate planning. Annual financial plans follow the longer-term financial strategy.
Finance for decision making	Top managers review the costs and benefits of allocating resources to different activities before they complete strategic and corporate plans. Managers thoroughly understand the financial implications of current and alternative policies, programmes and activities.
Financial monitoring and forecasting	Financial information and performance information are integrated. Top management is assured that financial performance and forecasts are in line with the plan. Monitoring and review of the underlying costs of the organisation’s key activities shows value for money or identifies issues for improvement.
Financial reporting	There is accurate, current, financial and non-financial performance information for all who need it.

Source: Audit Commission

**16** Table 2 illustrates some of the consequences of weak financial management, and the impacts on taxpayers, service users and councils.<sup>i</sup>

**17** Councils that follow the principles of good financial management are in a stronger position to provide services to taxpayers, deliver their priorities and objectives, and demonstrate financial resilience (Table 3).

<sup>i</sup> The case study examples in Table 2 are drawn from use of resources assessments and discussions with the councils concerned.

Table 2: Lack of good financial management is quickly visible

Area of financial management weakness	Case study example	Result
Financial governance and leadership	A district council failed to manage within its financial capacity and used reserves to subsidise spending on services in 1999. The council's reserves fell from £7m to £1m in four years and the council's accounts were qualified for three years.	No financial resilience
Financial governance and leadership	A district council sought to boost local employment by spending £4m to build new office accommodation for a new unitary authority in 2006. But it failed to do a proper risk assessment. Reorganisation fell through and the council now has an asset it cannot afford. The council has cut local services and closed a leisure centre to compensate.	Waste of taxpayers' money, reduced services
Financial planning	A district council failed to make the best use of its core grant funding. Instead, it bid for funding to deliver pilot projects or programmes that were never adopted. Until 2009 the council wasted money on bidding for projects that did not reflect local priorities or improve services.	Diverting resources from priorities
Finance for decision making	A unitary council was historically cash-rich. Until 2008 it over-provided statutory services and funded discretionary activities generously. The council failed to recognise a changing financial environment and regularly overspent its budget. The council's approach to financial management had three main weaknesses: <ul style="list-style-type: none"> <li>■ inconsistent analysis and understanding of costs;</li> <li>■ failure to benchmark or analyse value for money; and</li> <li>■ failure to assess whole-life costs and benefits of significant investments.</li> </ul> <p>Council tax rates are consistently higher than the unitary council average.</p>	High level of council tax
Finance for decision making	A unitary authority failed to test the value for money of its decisions. The council accepted all requests for child placements without considering other choices. In 2009/10, the council finally changed its approach following an analysis showing poor value for money and few positive outcomes for children.	Poor value for money
Financial monitoring and forecasting	A district council built its reserves and balances up to 31 per cent of Gross Revenue Expenditure between 2005 and 2008, without a plan for using them. Missed opportunities to invest resources led to ineffective and costly services.	Weakened service levels

Source: Audit Commission

Table 3: **Good financial management delivers better value for money**

Financial management principle	Case study example	Result
Financial governance and leadership	A unitary council recognised that it needed to improve its financial management. The chief executive and finance director work in partnership to set the strategic direction. They ended a practice of overspending on departmental budgets and introduced restructuring and efficiency measures.	Savings of £19m in 2008/09
Financial planning	A metropolitan district carried out a zero-based review of spending. The council used the results to assess how services met national and local priorities and delivered value for money.	This council moved from the highest council tax in the country in 2001/02 to the 37th lowest in 2008/09.
Finance for decision making	A district council recognised that current spending levels meant it would subsidise its current spending by £500,000 a year by drawing on its reserves. The council changed its long-term financial and corporate plans and aims to remove the reliance on reserves by 2011/12.	The council has adapted its change programme to deal with the recession and to ensure financial resilience. It plans to save £2.5m by 2011/12.
Financial monitoring and forecasting	A county council used the outcome of a scenario planning and financial forecasting exercise to develop a three-year plan to save £88m. The council is taking a strategic approach. It aims to fill a funding gap with the least impact on front-line services. The council expects to deliver savings through: <ul style="list-style-type: none"> <li>■ procurement restructuring and improvement;</li> <li>■ introducing vacancy control;</li> <li>■ restructuring all departments (removing 470 posts);</li> <li>■ introduction of a new HR and payroll system; and</li> <li>■ reducing corporate services spending.</li> </ul>	The council will save £29m in 2010/11.

Source: Audit Commission

# Getting fit for the future

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**Council income is under pressure, but demand for services continues to increase. Councils will have less money from government grant, frozen council tax income and reduced income from local fees and charges. They still have to deliver a balanced budget, exercise stewardship over public money and provide key front-line services. This chapter sets out the rationale for taking a long-term, strategic approach to managing money and planning services.**

### **Developing a long-term approach**

**18** Councils have tough decisions to make. They have to review priorities and reassess their definitions of front-line services to fit their reduced income. They should review their role in providing services, working with other local public bodies and stimulating local and community initiatives to fill the gaps. These changes require strong financial leadership and may mean a significant change in attitudes.

**19** Councils need to manage well by making sure that members, managers and staff understand the financial impact of objectives, priorities and actions. The principles of good financial management (Ref. 8) should guide councils' short, medium and long-term management of money.

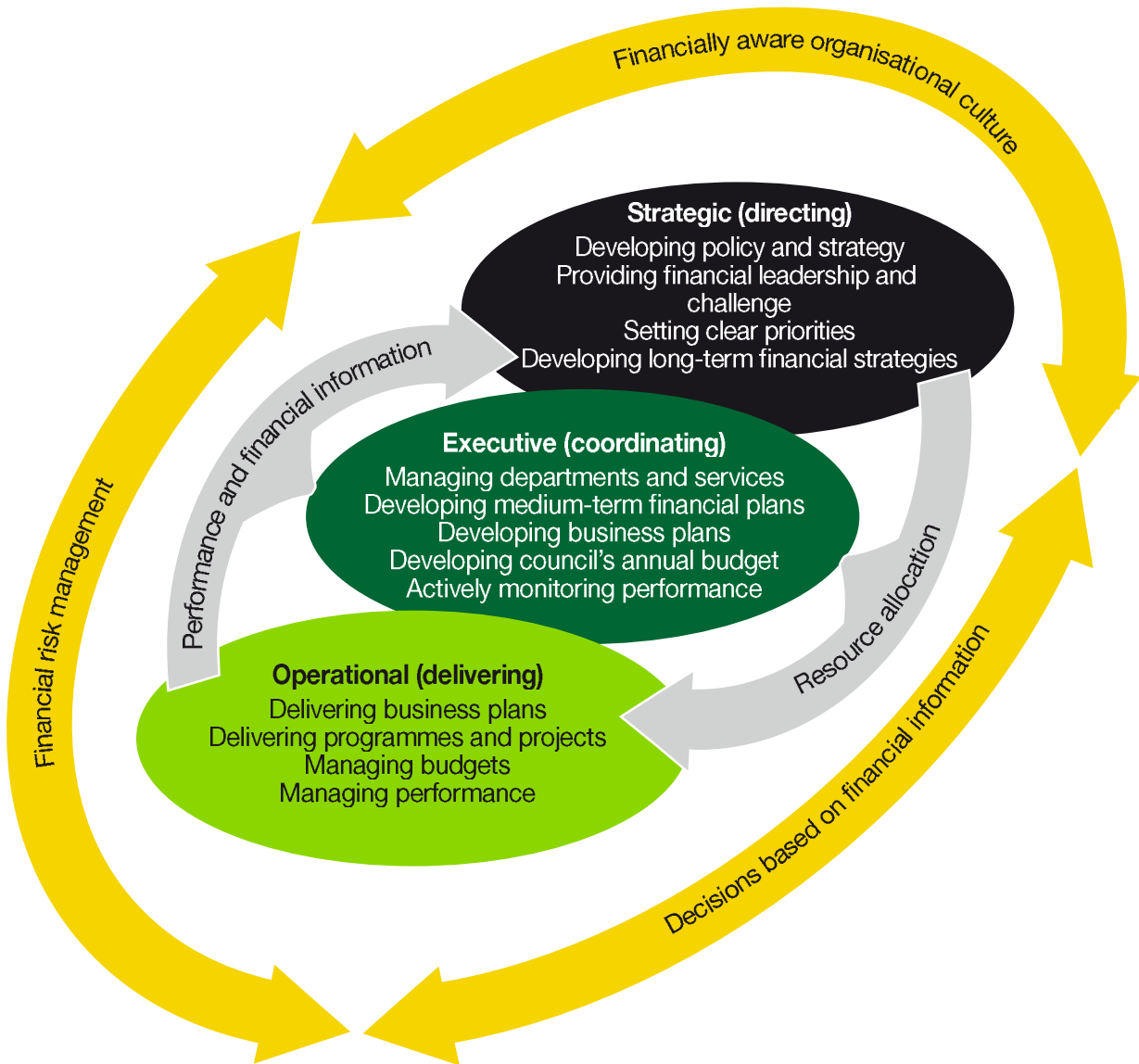
**'... the impression that the financial strategy exists on its own ... [is] not the right impression. It is inextricably linked to the council's corporate plan. It determines what's affordable and therefore what we're capable of delivering.'**

Workshop participant<sup>i</sup>

**20** Councils can deliver good financial management and prepare for an austere future by adopting a strategic approach to direction, coordination and delivery (Figure 1).

<sup>i</sup> As part of the fieldwork we conducted business narrative workshops with senior officers and elected members to understand councils' journeys towards a strategic approach to financial management. Full details of our methodology can be found in Appendix 3.

Figure 1: Good financial management is at the heart of an effective council



Source: Audit Commission

**21** This approach – strategic financial management (SFM) – is not an alternative to making tough financial decisions: it is the framework for making them.

**'[SFM]...is the lifeblood of the organisation.'**

Workshop participant

**22** Councils that manage money strategically can demonstrate five characteristics (Table 4):

- strong and accountable financial leadership;
- an organisational culture of financial awareness;
- an ability to specify priorities and make choices within means;
- comprehensive financial information that clearly underpins decisions; and
- an ability to anticipate changing circumstances and manage financial risks.

**Table 4: The five characteristics of strategic financial management**

Characteristic	Evidenced by
Strong and accountable financial leadership	The council leader and the chief executive set direction: they are accountable for achievement.
	The council leader and the chief executive agree their roles and responsibilities.
	The finance director and member with lead responsibility for finance are active members of the council’s leadership team.
A culture of financial awareness	Members and staff are aware of the financial results of their decisions and actions.
	Staff understand how their roles contribute to the council’s priorities.
	In-year savings are encouraged.
	Officers and members trust one another and productively challenge financial decisions.
An ability to specify priorities and make choices within means	Council and operational priorities are clear, few in number and affordable.
	Resource distribution aims to achieve priorities and deliver value for money.
	The council clearly communicates its priorities internally and with partners.
Comprehensive financial information that clearly underpins decisions	Financial and performance information is relevant, of a high quality and well presented.
	Important decisions have a business case that includes discussion of short, medium and long-term consequences.
	The expected financial and performance benefits of decisions are monitored.
An ability to anticipate changing circumstances and manage financial risks	The council is risk aware rather than risk averse.
	The council’s planning system recognises the potential financial impact of corporate risks.
	Opportunities that carry risks are managed actively.

*Source: Audit Commission*

## Taking stock

**23** Many people in the councils that have a long-term strategic approach to financial management recall the event that triggered their current approach. The four main triggers of change are:

- new political leadership following elections or changes among elected members;
- new managerial leadership following staff changes;
- internal reassessment following a critical audit or inspection report; or
- a serious financial or performance challenge.

**‘You can’t be strategic in your finances if you don’t know what you’re trying to achieve. That sounds completely self-evident but there are plenty of organisations that look year to year or don’t look more than a year or two ahead.’**

Chief Executive

**Financial challenge will accelerate decision making, but it will not make the process any easier.**

**24** All councils now face a serious financial challenge as income falls and financial resilience comes under greater stress. Councils need to deliver savings now. This will accelerate decision making, but it will not make the process any easier. Councils should ensure that short-term decisions do not undermine valuable long-term opportunities (Ref. 7). They will only be able to get the most from fewer resources if spending focuses on achieving strategic goals and money is managed effectively.

**25** Just four of the fourteen councils visited for this report displayed all five strategic financial management characteristics. Some councils had already recognised the need to improve. Seven of the councils were improving financial management, but three had not yet made plans to change. Councils with less well-developed long-term approaches can still act quickly to adopt and adapt the approaches taken by their high-performing peers.



# Making change happen

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**This chapter shows how councils can develop an effective approach to financial management. It describes each of the five SFM characteristics and shows how councils have adopted them. Leadership and culture are the foundations of a strategic financial approach; they underpin the fundamental organisational and process changes that will be needed over the next few years. Councils can start work on strengthening leadership and culture before they follow through by developing choice, decision making and risk management.**

### **Strong and accountable financial leadership**

**Strong and accountable financial leadership starts at the top of the council.**

**26** Strong and accountable financial leadership starts at the top of the council and sets the tone for all strategic, executive and operational activity. The council leader and the chief executive work together to set the direction; they recognise their shared accountability for achievement. The finance director and the elected member with lead responsibility for finance should be active members of the council's leadership team. Success follows from an understanding and recognition of each other's roles, responsibilities and constraints.

**27** A council's financial leaders can ensure:

- regular, constructive challenge of financial assumptions and direction;
- open and honest discussion about what is desirable and what is affordable;
- clear responsibility and accountability;
- understanding of the current financial position and potential future opportunities and threats;
- that information is used to make evidence-based decisions and to manage performance; and
- regular, dedicated time for them to focus on the strategy.

**28** Effective leadership is an imperative when resources are scarce. CIPFA's paper *Leading in Hard Times* (Ref. 7) describes how leaders can manage current and future challenges. CIPFA suggests that leaders need to set and communicate a long-term vision supported by clear specification of how reduced resources will be allocated in the short to medium term.

**29** Many councils are introducing stronger and more accountable financial leadership. Eight of the fourteen councils visited had strong financial leadership. The remaining six councils lacked this key element of strategic financial management.

## Case study 1

### Building strong financial leadership

A county council lacked clear financial leadership and experienced several financial management failures.

- Members of the senior management team lacked relevant financial qualifications.
- The council did not use the finance system, introduced in 2001, to its full potential.
- The council received a qualified set of accounts in 2002/03 following a significant failure of internal financial control in one directorate.
- External auditors advised that general reserves were too low in 2003/04.
- A 2004 independent review, using CIPFA's Financial Management Model (Ref. 10), criticised the council's performance.

A change in administration in 2005 coincided with changes in the leadership team. A new finance director (FD) started in 2004 and a new chief executive (CEO) followed in 2005. They recognised and acted to address the financial problems. The CEO, with support from the council leader, changed the management structure and the FD joined the corporate management team. The CEO introduced a new performance management system and backed a drive by the FD to improve financial awareness through compulsory training. The council leader and the member with lead responsibility for finance had financial experience and the respect of local and regional peers. The partnership between the members of the leadership team has delivered a strong focus on financial prudence and improvement across the council.

A star chamber focuses spending on delivering the council's strategic objectives. The medium-term financial strategy sets out service objectives and is the planning framework for annual budgets. Clear service and resource planning has enabled the council to improve value for money and deliver savings of £30m since 2006.

*Source: Audit Commission*

## An organisational culture built on financial awareness

**30** Elected members and council staff should be aware of the financial effects of their decisions and actions, and they have to trust one another to act responsibly. The leadership team should establish and maintain a culture that requires and enables staff to take collective and individual responsibility for the stewardship of funds – and for delivering value for money.

**31** The leadership team can begin to establish a financially aware culture by clearly communicating the long-term financial strategy, the current position, likely challenges and proposed solutions to staff and external stakeholders. This approach will help staff to understand how their roles contribute to the council’s priorities.

**32** Many staff and elected members will need support to develop financial skills and understand the principles of financial management. The translation of financial principles into the management of everyday activities is at the core of a financially aware culture.

**33** It takes time to create a financially aware organisation, but there are clear benefits (Table 5).

Table 5: The benefits of being a financially aware organisation

Benefit	Case study example
Staff consider financial impacts before deciding to act. They evaluate and challenge decisions and can identify better ways to deliver services.	Elected members in a district council encourage staff to review internal and external drivers of costs or demand. Staff identify opportunities to improve service delivery and improve value for money. A contract retendering suggested by staff in 2008 saved £650,000.
Staff understand how their work contributes to the activities of the council.	A district council has a ‘golden thread’ that links its strategic, executive and operational plans. The policy and performance management framework, introduced in 2001, ensures staff understand their priorities and challenges. The framework guides performance measurement throughout the council. It links area objectives to staff performance objectives. The council provides financial training, workshops and regular briefing sessions to staff and elected members.
In-year savings are realised.	A district council reduced overhead costs from £92 to £11 per transaction in 2008/09 by introducing procurement cards in all service areas.

Benefit	Case study example
Elected members and staff provide regular and productive challenge to planning assumptions and service delivery choices. This leads to better use of information, ownership of decisions and greater resilience.	A district council’s members insist on extensive scenario planning and they challenge their own and officers’ assumptions. Directors look ahead at risks and opportunities. The council introduced a three-year programme to reduce carbon emissions and energy costs in 2008. New boilers and solar panels have cut heating bills by 15 per cent. More efficient computers have cut IT electricity bills by 90 per cent.
Improved productivity	A county council introduced a shared service centre in 2007. The business case required spending £4.2m to produce savings of £27m over eight years. Improved technology and working practices have enabled the council to reduce the service centre workforce by 250. The remaining workforce has lower turnover and lower sickness levels. The proportion of staff taking sick leave is below average. External customers are happier with the new service.

Source: Audit Commission

**34** Many councils need to take urgent action to help staff improve their financial awareness. Six of the fourteen councils visited had developed an organisational culture built on financial awareness. However, financial awareness was underdeveloped in the other eight councils.

**Case study 2**

**Building a culture of financial awareness**

A county council experienced serious financial challenge:

- finance did not match need – the council had below-average income, but above-average demand for services;
- front-line services, including social care and education, were underfunded; and
- back-office systems, including finance and ICT, were outdated and inefficient.

A £3m unexpected overspend in adult social care was the trigger for improvement. The council recognised that staff did not identify, understand or manage financial risks. Management information was poor and rarely used.



The council's leadership team's first step was to improve financial awareness among staff and councillors. The council provided financial awareness training and introduced a performance management system. All staff who make financial decisions have performance targets linked to corporate and service objectives.

The council also improved the production, quality, clarity and use of finance and performance information. Staff use information on service costs and benefits, service delivery options, current and future financial risk, and benchmarking information to support decisions.

The leadership team introduced an annual review of performance and efficiency to ensure that activities link to corporate objectives. Annual reviews also identify areas of poor performance and opportunities for improvement. Senior staff and councillors work together to set priorities and challenge financial decisions. The medium-term financial plan is reviewed regularly.

The council has improved outcomes in all services and began to prepare for a reduced income in autumn 2009. In-year savings of £25 million were made against the 2009/10 financial plan. The council plans savings of £45 million for 2011/12.

*Source: Audit Commission*

## Specifying priorities and choices within means

**35** A council's strategic priorities and its financial health are the framework for the council leader and chief executive to agree what is practicable. Together with the finance director and the portfolio holder for finance, they can ensure that resources are allocated to achieve priorities and deliver value for money.

**36** Strategic priorities should drive all council business, from service plans through to the performance objectives of individual staff. Accurate and detailed long-term financial strategies and medium-term financial plans can ensure the delivery of strategic priorities by enabling appropriate financial choices. Longer-term planning can also help councils overcome the constraints of the annual, or rolling 18-month planning and budgeting cycle. This short-cycle view encouraged an incremental and process-driven approach that is too inflexible during a period of rapid external change.

**Strategic priorities should drive all council business, from service plans through to the performance objectives of individual staff.**

**37** Use of resources judgements between 2005 and 2008 illustrated widespread improvement in the development of medium-term financial strategies (Ref. 6, Ref. 11). Eight of the fourteen councils visited for this study considered longer-term financial implications when setting priorities and making choices. Two councils only partly took account of these issues and four did not consider them at all.

**38** In the absence of long-term plans, councils will rely on medium-term plans (three to five years) to support the delivery of their priorities, identify potential risks and assign responsibilities. An analysis of medium-term financial plans from 2005/06 to 2009/10<sup>i</sup> shows increased links to other strategic planning documents, such as corporate strategies, capital investment plans and asset management plans. The quality of medium-term financial plans varies, however, and there are concerns that need to be addressed (Table 6).

Table 6: **There are gaps in medium-term financial plans (MTFPs)**

Feature	Concerns
Outcome measures	Half of the 42 plans reviewed for this paper did not contain any outcome measures. Nine of the plans included both financial and non-financial outcome measures.
Scenario planning	Only seven plans included scenario planning, of which five considered best and worst-case scenarios.
Costs and overheads	28 out of 42 plans did not distinguish between the behaviours and relationships of variable and fixed costs.
Benchmarking	26 out of 42 plans did not include cost benchmarking against other councils or value-for-money (VFM) indicators.
Resource planning	Only eight plans referred to workforce strategies.
Partnership working	Half of the plans had no information, financial or otherwise, about joint plans.

*Source: Audit Commission*

<sup>i</sup> For this research we reviewed 42 medium-term financial plans from a cross-section of 34 councils.

### Case study 3

## Specifying priorities and making choices

In 2001, a metropolitan council recognised that high levels of council tax were unsustainable and that spending needed better management. The top team focused on streamlining service delivery, achieving a neutral budget (no growth above the rate of inflation) and setting annual council tax increases of no more than 2.5 per cent.

The council did a zero-based budget review of all services to assess spending and identify opportunities to make savings. The review prompted the council to change its financial planning arrangements to focus on delivering the strategic priorities. Service directors had to find ways to deliver better value for money, including service transformation. The council created a rolling fund, using earmarked reserves, to cover the early costs of delivering change. The council used the fund to deliver personalised social care by sequentially closing down older people's homes and replacing them with independent living accommodation.

The council now takes a longer-term approach to financial planning. It models and forecasts risks and opportunities over a ten-year period. The council began preparing for a 10 per cent cut in its budget by 2012/13 in October 2009. It took account of budget cuts, increasing service demands, and increased national insurance and pension payments to arrive at a savings target of £25m. The council now has a business transformation group to oversee the savings programme and identify the bigger savings needed to work within a much-reduced financial settlement.

*Source: Audit Commission*

## Comprehensive financial information clearly underpins decisions

**39** Decision makers at all levels need to recognise why financial information is important and how they can use it to:

- make informed decisions;
- manage performance; and
- review past decisions to ensure that expected financial and performance benefits are realised.

**40** Decision makers need relevant, high-quality information that enables them to balance priorities and resources.



**‘Successful strategies ... are the end product of a structured and disciplined decision-making process.’**

*CIMA, Maximising Shareholder Value: Achieving Clarity in Decision-Making, 2004.*

**41** Information should be comprehensive, relevant, of a good quality and well presented (Ref. 12). As a minimum, financial information should include details of financial trends, suitable benchmarking information, possible scenarios and their likely impact over the short, medium and long term. Councils should consider producing and using information on:

- financial and performance trends, including benchmarking data and whole-life costs;
- costs of service delivery and the influence of different cost drivers;
- analysis of current and future pressures, including realistic scenario planning for possible socio-economic changes and their impact;
- horizon scanning for any unexpected national (or international) changes that may affect the council; and
- short, medium and long-term risks associated with presented choices and costed risk management strategies.

#### Case study 4

### Using information to make decisions

A district council places a strong emphasis on economic development and regeneration, delivered through a programme of capital projects and financial investment. The council takes an informed, long-term approach to financial management. It introduced medium-term financial planning in 2002 before central government introduced three-year funding, and it routinely conducts financial modelling and scenario planning over five and ten-year periods.

The council produces financial information that is easily understood and trains councillors and staff to make the best use of it. The council has worked to make financial and performance documents readable, accessible and jargon-free. Good use of information underpins a policy and performance management framework that drives and informs performance throughout the organisation.

*Source: Audit Commission*

**42** Many councils can improve their use of information. Eight of the fourteen councils visited made clear use of financial and other information to inform their financial decisions. But arrangements were underdeveloped in two councils and absent in four.

Case study 5

### Using information to make decisions

A unitary council uses performance information to support strategic and operational decisions. Scenario plans enable councillors to try out possible choices, savings and decisions. Scenario plans created in 2009/10, included discussion of the implications of a possible 30 per cent fall in grant and 2 and 4 per cent increases in council tax. The analysis estimated a funding gap of £14m in 2010/11. The council started to plan for savings well before the emergency budget.

*Source: Audit Commission*

### An ability to anticipate changing circumstances and manage financial risks

**43** Councils need to manage with reduced income. They need to decide quickly how to make savings; but speed will not make the decisions any easier. Councils can ensure that the right decisions are made by ensuring they understand their priorities, costs and associated risks. The potential financial impact of corporate and other risks should be incorporated into financial plans.

**‘Risk management is a central part of any organisation’s strategic management. It is the process whereby organisations methodically address the risks attached to their activities with the goal of achieving sustained benefit within each activity and across the portfolio of all activities.’**

AIRMIC, ALARM, IRM,  
*A Risk Management Standard, 2002.*

### Expecting and managing financial risks for the short, medium and long term underpins good financial management.

**44** Expecting and managing financial risks for the short, medium and long term underpins good financial management. A planned approach is more likely to be risk aware rather than risk averse.

**45** Opportunities that carry risk should not simply be ruled out: they should be managed. Councils can use financial and other information to base their decisions on the impact, likelihood and potential financial effects of risks.

## Case study 6

### Conducting detailed risk assessments

A unitary council conducts a detailed risk assessment of the key issues affecting each service. The council's research and intelligence unit uses demographic information to anticipate demand for different services (for example, benefit claimants and car park users). This information is combined with benchmarking data to inform the level of risk, which is managed through the reserves. In 2009/10 risks were valued at £8 million.

The finance director has a clear view of the role of finance in risk assessments:

**'The whole purpose [of risk assessment] is to determine a value attached to the risks so it can inform my view on a recommendation on reserves and contingencies.'**

*Source: Audit Commission*

**46** There is scope for councils to improve financial risk management. Just five of the fourteen councils visited actively anticipated and managed financial risks. Arrangements were underdeveloped in six councils and absent in three more.

**47** Few councils had anticipated or planned for a cut in their 2010/11 budget and scenario plans in the councils visited were limited in their scope. Scenarios rarely consider more than three to five years ahead, or decreases in government grant of more than 10 per cent. Just one of the fourteen councils visited had considered possibilities up to a 30 per cent decrease in government grant.

**48** Councils cannot predict that proportion of their income that relies on central government beyond the current settlement. But they can use information to anticipate changing circumstances, set priorities, make choices and manage delivery. They can calculate how much they would need to deliver current services (at current or future prices) and review alternative income and spending scenarios to identify gaps and prepare for the future by investigating different approaches (Ref. 9).

Case study 7

### Expecting and managing financial risks

A unitary council uses a red, amber, green rating system to assess and manage financial risk. Risk planning and management is part of medium-term financial planning. There are strategic and service-based risk assessments. Service plans cover financial risks and opportunities. Actions are classified as level 1 (higher risk, requiring extra resources and therefore closer monitoring) and level 2 (do not require extra resources and lower risk).

The finance team and service managers use financial modelling to identify risks related to increased demand for services. They test and review new ways of working to mitigate new or increased risks, such as the likely impact of an ageing population on adult social care costs. A named member of the finance team manages each major risk.

The council also reviews the impact of service plans on future asset and staffing levels. The council is the largest local employer and the risk assessment includes consideration of any potential impact of job losses on the local economy.

The council's first assessment of the risks posed by a decline in government grant identified a £14 million funding gap and options to deliver savings in year 2009/10.

*Source: Audit Commission*

# What is your council doing?

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Evaluate financial management and make changes	30
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**This chapter will help councils to assess how well they are managing money in the changed economic circumstances and identify improvements needed to achieve good outcomes for the short, medium and long term.**

### **Evaluate financial management and make changes**

**During times of stress, and to avoid them becoming times of crisis, there must be clarity about responsibilities for tackling the financial challenge.**

**49** During times of stress, and to avoid them becoming times of crisis, there must be clarity about responsibilities for tackling the financial challenge. Councils have to be clear about how they will evaluate their current practice and how they will begin to improve.

**50** Appendix 1 includes a good-practice checklist based on the five characteristics of SFM (a separate downloadable version is at [www.audit-commission.gov.uk/SFMA1](http://www.audit-commission.gov.uk/SFMA1)). The checklist suggests the key issues that councils should consider for improving their financial leadership, financial awareness, financial capacity, use of information and financial risk management.

**51** The checklist also describes common problems that arise when councils fail to adopt a strategic approach. Councils can use the checklist, together with the case study examples in Chapter 3, to evaluate their current approach to financial management.

**52** The government's 2010 Spending Review Framework set out nine questions for Whitehall departments (Ref. 5). Equivalent questions for councils are:

- how is this activity essential to achieving council priorities?
- how does this activity improve the wellbeing of local communities?
- why does the council need to fund this activity?
- how can we focus this activity on people most in need?
- how can we provide this activity at lower cost?
- what can make this activity more effective?
- which other local bodies could provide this activity?
- how can the private sector, third sector or citizens provide this activity, whole or in part?
- how can we make sure that payment to service providers links to achievement?

**53** These local challenge questions are included in a self-assessment checklist (Appendix 2). A downloadable version is available at [www.audit-commission.gov.uk/SFMA2](http://www.audit-commission.gov.uk/SFMA2). The self-assessment can help councils review and challenge their activities from first principles. The characteristics of strategic financial management can then provide the framework for dealing with weaknesses identified through the self-assessment.

## Conclusion – can you afford not to?

**54** Councils need to make some urgent and tough decisions. A fall in income requires them to make cuts today, while safeguarding key front-line services for the future.

**Councils need to make some urgent and tough decisions.**

**'We used to think the strategy came first and then the budget followed. Now we know the reality. You have ambitions, then you look for resources and find you cannot afford the ambitions quite as you had hoped.'**

Chief Executive

**55** SFM enables councils to align priorities and finances. SFM ensures that councils make the right strategic and financial decisions to address the challenges of today, make changes to service delivery and plan for the long term.

**56** Effective strategic financial management takes strong and accountable leadership and a financially aware organisation that sets clear priorities, uses information and manages risk. Some aspects of SFM can be adopted quickly. Others will take longer to realise. But the effort is worth it.

**57** Councillors and senior managers should use this paper to test and challenge their plans. Failure to act will not go unnoticed by citizens, taxpayers and service users.

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## Appendix 1: Good-practice checklist

### The checklist

Councillors and senior managers can use this good-practice checklist to examine their financial management arrangements. The checklist is designed to help councillors and senior managers follow the principles of strategic financial management (SFM). It outlines issues to consider and common problems for each of the five characteristics of SFM. The checklist will help councillors and senior managers to identify strengths and weaknesses for their council and identify issues for further investigation and improvement.

### Using the checklist

The leadership team could use the checklist to:

- evaluate the council’s strengths and weaknesses in financial management;
- improve the discussions on council strategy;
- provide the agenda for a strategy conference;
- introduce a longer-term approach to financial management; or
- support organisational transformation.

The indicators of success could also be translated into actions and objectives for change.

### Adopting strategic financial management – a checklist

Indicators of success	Potential problems
<b>Characteristic one: Strong and accountable financial leadership</b>	
The council leader and the chief executive work together to set the council’s direction.	No agreed long-term vision for the council Lack of support for the corporate direction
The council leader and chief executive are jointly accountable for achievement.	Unclear accountability
The finance director (and elected member with lead responsibility for finance) is part of the leadership team.	The finance director is not part of the leadership team.
There is clear understanding of respective roles, responsibilities and constraints.	Lack of understanding of roles and responsibilities
	Little common understanding among officers and members
The leadership team ensures that: <ul style="list-style-type: none"> <li>■ there is regular, productive challenge of financial assumptions and direction;</li> <li>■ there is open and honest discussion about what is desirable and what is affordable;</li> <li>■ responsibility and accountability are clear;</li> <li>■ that information is used to make evidence-based decisions and to manage performance;</li> <li>■ leaders understand the current financial position and potential future opportunities and threats; and</li> <li>■ there is regular, dedicated time for leaders to focus on the strategy.</li> </ul>	The council lacks systems that enable robust and constructive challenge.
	Internal disputes or interests undermine attempts to plan
	Lack of transparency in decision making
	Lack of understanding of the current financial position and potential future implications
	A focus on thinking and operating only in the short term

Indicators of success	Potential problems
<b>Characteristic two: An organisational culture built on financial awareness</b>	
<p>The council has adopted a transformational approach. Elected members and council staff work together to achieve council goals.</p> <p>Staff are required and enabled to take collective and individual responsibility for the stewardship of funds and for delivering value for money.</p> <p>Elected members and council staff trust one another to act responsibly.</p>	<p>Protectionism of departmental budgets and working practices.</p> <p>Lack of trust, suspicion and internal disagreement on priorities.</p>
<p>Elected members and council staff are aware of the financial effects of their decisions and actions.</p>	<p>Finance officers work in silos with little regard for wider organisational priorities.</p>
<p>The leadership team clearly and decisively communicates the long-term financial strategy, the current position, likely challenges and proposed solutions to staff and to external stakeholders.</p>	<p>Poor communication of priorities and challenges.</p>
<p>Staff understand how their roles contribute to the council's priorities.</p>	<p>Officers and members do not know how their roles contribute to the council's priorities.</p>
<p>Staff and elected members are supported to develop financial skills and to understand the principles of financial management.</p>	<p>Financial literacy and knowledge is not rooted in the organisation.</p>
<b>Characteristic three: An ability to specify priorities and make choices within means</b>	
<p>The council leader and chief executive use the strategic priorities and financial position to decide what is practicable in the short, medium and long term.</p>	<p>Departments manage within their own priorities and budgets, without linking to corporate strategy.</p>
<p>The council leader and chief executive consider pressures such as demographic change, economic, environmental, legal and social challenges and future affordability when setting the council's strategic priorities.</p>	<p>No consideration of potential future pressures or challenges</p>
<p>The council leader and chief executive work with the finance director to ensure that resources are allocated to achieve priorities and deliver value for money.</p>	<p>Resource allocation is incremental, based on past budgets and limited performance information.</p>
<p>The strategic priorities drive all council business, from service plans through to the performance objectives of individual staff.</p> <p>Staff use financial strategies and plans to make financial choices and ensure the delivery of strategic priorities.</p>	<p>Departments follow individual priorities and keep their own reserves.</p>

Indicators of success	Potential problems
<p>The council produces accurate and detailed long-term (ten years or more) financial strategies and medium-term financial plans.</p> <p>Medium-term financial plans include:</p> <ul style="list-style-type: none"> <li>■ outcome measures;</li> <li>■ scenario plans;</li> <li>■ details of costs and overheads;</li> <li>■ comparative benchmarking information to assess costs and performance;</li> <li>■ links to other relevant council strategies such as workforce plans; and</li> <li>■ details of partnership activities.</li> </ul>	<p>Short-term planning within individual departments</p> <p>Medium-term financial plans are not reviewed and updated regularly.</p> <p>Realistic scenario planning not present</p> <p>Regular use of reserves to balance budgets</p>
<b>Characteristic four: Comprehensive financial information clearly underpins decisions</b>	
<p>Elected members and council staff understand why financial information is important.</p>	<p>Officers and members are not prepared to admit knowledge gaps.</p>
<p>Elected members and council staff understand how to use financial information to:</p> <ul style="list-style-type: none"> <li>■ make informed decisions; and</li> <li>■ review past decisions to ensure that expected financial and performance benefits are realised.</li> </ul>	<p>Lack of transparency in decision making</p>
<p>Elected members and council staff use relevant, high-quality information to make decisions.</p>	<p>Decisions are made without considering all relevant information.</p>
<p>Council staff produce information that is comprehensive, timely and easily understood.</p>	<p>Financial resources are not clearly allocated to corporate priorities.</p>
<p>As a minimum, financial information includes details of financial trends, suitable benchmarking information, possible scenarios and their likely impact over the short, medium and long term.</p>	<p>Decisions are based on short-term need, with little or no consideration of long-term consequences.</p>
<b>Characteristic five: An ability to anticipate changing circumstances and manage financial risks</b>	
<p>Financial risk management is an integral part of the council's activities.</p>	<p>All financial risks are given the same attention.</p>
<p>Financial plans include the potential financial impact of corporate and other risks.</p>	<p>Risk registers grow without clear policies on prioritisation or culling.</p>
<p>The council has anticipated and is mitigating the risks arising from reduced funding and increased demand.</p>	<p>The council does not understand the financial implications of its risks.</p>
<p>The council understands the difference between hazard and risk and is risk aware.</p> <p>Opportunities that carry risk are actively managed.</p>	<p>The council is risk averse rather than risk aware. Risks and opportunities of alternative service delivery mechanisms are misunderstood.</p>
<p>Scenario plans consider best and worst-case options and cover a wide range of financial and social challenges.</p>	<p>Financial risks are managed in the short term.</p>

## Appendix 2: Self-assessment questionnaire

### The self-assessment

This self-assessment questionnaire is based on the government’s 2010 Spending Review Framework questions for Whitehall departments (Ref. 5). These nine challenge questions divide into:

- three direction-setting questions for the leadership team;
- three coordinating questions for the senior management team; and
- three service management and delivery questions for service heads and managers.

### Using the self-assessment

Answers to the nine challenge questions can help councils review how they will deliver their priorities with reduced resources and still achieve value for money.

Each set of three questions is supplemented by ‘issues to consider’. These are additional questions that can help focus attention. These

issues are not exhaustive. One of the key challenges for councils is to improve their understanding of how the questions relate to local issues and priorities.

The self-assessment questions are aimed at different levels of management. But this should not exclude councils from adapting them for use with elected members, citizens, communities and other stakeholders. The first three questions could equally be the starting point for a local strategic partnership discussion that led to all nine questions being considered.

All nine main questions and the issues that go with them are open-ended. It is impossible to answer ‘yes’ or ‘no’. This should ensure that the questions stimulate debate, discussion and new approaches to the challenges faced by councils. In the longer term the questions can also help councils consider the mechanisms and culture that will lead to a more strategic approach to financial management – especially if the answer to any question is ‘don’t know’.

### Nine challenge questions

Answers to the questions higher up the list shape answers to the questions lower down.

Challenge questions	Issues to consider	Lead responsibility
<b>Setting the direction</b>		
1. How is this activity essential to achieving council priorities?	What are our priorities (and non-priorities)? How do our financial plans support our priorities?	Council leader
	Do we direct resources in line with priorities (rather than use crude proportional cuts to make savings)?	Chief executive Finance director
2. How does this activity improve the wellbeing of local communities?	What do we expect to happen over the next five to ten years and how will we prepare for it?	Portfolio holder
	How do we use modelling or scenario planning to improve our long-term vision and strategy? How well do we consider long-term risks?	
3. Why does the council need to fund this activity?	How well do we use performance and cost measures to highlight activities for radical rethinking of management and delivery?	
	What are the alternative approaches to funding activities?	

Challenge questions	Issues to consider	Lead responsibility
<b>Coordinating activities</b>		
4. How can we focus this activity on people most in need?	How well do we use unit costs, activity costs, benchmarks and other financial performance measures to support decisions about the council's portfolio of services?	Service directors Service heads
5. How can we provide this activity at lower cost?	How well do we use evidence to choose among targeted, preventive and universal provision?	Portfolio holders
6. How can we make this activity more effective?	Do we review our business models often enough to respond to the changing environment and new ideas?  How effectively does our organisational culture recognise and reward efficiency and cost reduction?  How can overview and scrutiny take a stronger role in challenging decisions?	Committee chairs
<b>Service management and delivery</b>		
7. How can other local bodies provide the activity?	How often are services challenged and subject to end-to-end review? How robust are predictions of savings and other benefits?	Service heads Service managers
8. How can the private sector, third sector or citizens provide this activity in whole or part?	Which other local public bodies could provide the activity? What would be the best way to transfer or share responsibility (contracts, aligned or pooled budgets, lead professional or personal budgets)?  Which voluntary groups, social enterprises or private sector organisations could provide this activity?	
9. How can we make sure that payments to providers link to achievement?	How would these arrangements be managed? What would be the best way to manage the transfer of responsibilities?  How well does the council understand the current market for this service? What can be done to stimulate the market?  What improvements are needed to ensure commissioning and procurement processes deliver the best service management and delivery arrangements?  What measures does the council need in order to effectively challenge performance weaknesses by any providers?  How does the council ensure that promised financial and performance benefits are realised and rewarded?	

*Source: Audit Commission*

## Appendix 3: Method

The research for this paper included four work strands.

- A review of existing guidance on strategic financial management. The review included guidance from central government, professional associations and academic sources. The review provided the core concepts for this paper's identification of the key features of strategic financial management.
- Analysis of Use of Resources (UoR) data and local government financial time series data.<sup>i</sup> Councils' reserves, debts, income and spending, alongside demographic and economic pressures, have been examined to test how far financial strategies and plans have influenced financial and other decisions.
- An examination of 42 medium-term financial plans from a cross-section of 34 councils. This assessed how councils have approached financial planning over the last five years and included councils identified by auditors as being good, improving or poor in their approaches to strategic financial management.
- Fieldwork with councils selected from their 'managing finance' UoR score (2007/08 and 2008/09), and auditors' and CAA leads' recommendations. The Audit Commission is grateful for the time and information given by these councils.
  - Researchers visited 14 councils (a mixture of single tier, district, and county councils). The visits included interviews with senior officers and elected members. The interviews explored how councils make strategic financial decisions and their preparations for the medium to long-term challenges of the current economic situation.

- In a further four councils, business narrative workshops were held to discuss leadership and culture questions and to track those councils' journeys towards a strategic approach to financial management.

The following councils helped with the research.

- Basingstoke and Deane Borough Council
- Borough of Broxbourne
- Hambleton District Council
- Merton London Borough
- North Kesteven District Council
- Nottingham City Council
- Nottinghamshire County Council
- Oxfordshire County Council
- Peterborough City Council
- Ryedale District Council
- St Helens Metropolitan Borough Council
- Stockton-on-Tees Borough Council
- Tameside Metropolitan Borough Council
- Warwick District Council
- Waverley District Council
- West Berkshire Council
- Wigan Metropolitan District Council
- Worcestershire County Council

The five strategic financial management characteristics derive from World Class Financial Management (Ref. 8) and the review of other existing guidance on strategic financial management. The five characteristics were tested through the interviews with senior officers and members and through:

- an analysis of council documents and plans;
- a cross-check against our analysis of local government financial time series data; and
- peer review and challenge from senior auditors.

Agnieszka Scott project managed this study, supported by Faye Joshua, Paul Honeyben, Laura Holloway, Sumithra Rabindrakumar and Tony Whitehead. Karen Price provided administrative support. Sarah Furlong and Michael Hughes were respectively the head of studies and director for this study.

<sup>i</sup> Income data from CLG Local government finance statistics: [www.communities.gov.uk/publications/corporate/statistics/financialstatistics192009](http://www.communities.gov.uk/publications/corporate/statistics/financialstatistics192009) and spending data from revenue and capital outturn returns: [www.communities.gov.uk/documents/statistics/pdf/1401553.pdf](http://www.communities.gov.uk/documents/statistics/pdf/1401553.pdf); and [www.communities.gov.uk/documents/statistics/pdf/13685721.pdf](http://www.communities.gov.uk/documents/statistics/pdf/13685721.pdf)



The external advisory group was:

<b>Group member</b>	<b>Organisation</b>
Ken Beeton	HM Treasury
John Benington	Warwick Business School
Nick Jackson	HM Treasury
Chris Lambert	National Audit Office
Neil Riddell	Communities and Local Government
Alison Scott	Chartered Institute of Public Finance and Accountancy (CIPFA)
Tony Travers	London School of Economics
Penelope Tuck	Warwick Business School

We also consulted with representatives from Society of Local Authority Chief Executives, Communities and Local Government, Local Government Association, Society of District Council Treasurers, Society of County Treasurers, Society of London Treasurers and Society of Metropolitan Treasurers. We discussed our emerging findings with 75 senior finance professionals from English local authorities during five CIPFA Financial Advisory Network events in May 2010.

The Commission thanks all those who were involved and gave their opinions and time. However, the views expressed in this report are those of the Audit Commission alone.

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# **Strategic financial management in councils**

**Self-assessment questionnaire**

Local government, July 2010

# Self-assessment questionnaire

## The self-assessment

This self-assessment questionnaire is based on the government's 2010 Spending Review Framework questions for Whitehall departments (Ref. 5). These nine challenge questions divide into:

- three direction-setting questions for the leadership team;
- three coordinating questions for the senior management team; and
- three service management and delivery questions for service heads and managers.

This self-assessment questionnaire has been produced to support the Audit Commission's report *Strategic Financial Management in Councils: Delivering Services with a Reduced Income* that is available on the Commission's website at [www.audit-commission.gov.uk/SFM](http://www.audit-commission.gov.uk/SFM)

## Using the self-assessment

Answers to the nine challenge questions can help councils review how they will deliver their priorities with reduced resources and still achieve value for money.

Each set of three questions is supplemented by 'issues to consider'. These are additional questions that can help focus attention. These issues are not exhaustive. One of the key challenges for councils is to improve their understanding of how the questions relate to local issues and priorities.

The self-assessment questions are aimed at different levels of management. But this should not exclude councils from adapting them for use with elected members, citizens, communities and other stakeholders. The first three questions could equally be the starting point for a local strategic partnership discussion that led to all nine questions being considered.

All nine main questions and the issues that go with them are open-ended. It is impossible to answer 'yes' or 'no'. This should ensure that the questions stimulate debate, discussion and new approaches to the challenges faced by councils. In the longer term the questions can also help councils consider the mechanisms and culture that will lead to a more strategic approach to financial management – especially if the answer to any question is 'don't know'.

## Nine challenge questions

Answers to the questions higher up the list shape answers to the questions lower down.

Challenge questions	Issues to consider	Lead responsibility
<b>Setting the direction</b>		
1. How is this activity essential to achieving council priorities?	What are our priorities (and non-priorities)? How do our financial plans support our priorities?	Council leader
	Do we direct resources in line with priorities (rather than use crude proportional cuts to make savings)?	Chief executive Finance director
2. How does this activity improve the wellbeing of local communities?	What do we expect to happen over the next five to ten years and how will we prepare for it?	Portfolio holder
	How do we use modelling or scenario planning to improve our long-term vision and strategy? How well do we consider long-term risks?	
3. Why does the council need to fund this activity?	How well do we use performance and cost measures to highlight activities for radical rethinking of management and delivery?	Portfolio holder
	What are the alternative approaches to funding activities?	
<b>Coordinating activities</b>		
4. How can we focus this activity on people most in need?	How well do we use unit costs, activity costs, benchmarks and other financial performance measures to support decisions about the council's portfolio of services?	Service directors
		Service heads
5. How can we provide this activity at lower cost?	How well do we use evidence to choose among targeted, preventive and universal provision?	Portfolio holders
	Do we review our business models often enough to respond to the changing environment and new ideas?	Committee chairs
6. How can we make this activity more effective?	How effectively does our organisational culture recognise and reward efficiency and cost reduction?	Committee chairs
	How can overview and scrutiny take a stronger role in challenging decisions?	

Challenge questions	Issues to consider	Lead responsibility
<b>Service management and delivery</b>		
7. How can other local bodies provide the activity?	How often are services challenged and subject to end-to-end review? How robust are predictions of savings and other benefits?	Service heads Service managers
8. How can the private sector, third sector or citizens provide this activity in whole or part?	Which other local public bodies could provide the activity? What would be the best way to transfer or share responsibility (contracts, aligned or pooled budgets, lead professional or personal budgets)?	
9. How can we make sure that payments to providers link to achievement?	<p>Which voluntary groups, social enterprises or private sector organisations could provide this activity?</p> <p>How would these arrangements be managed? What would be the best way to manage the transfer of responsibilities?</p> <p>How well does the council understand the current market for this service? What can be done to stimulate the market?</p> <p>What improvements are needed to ensure commissioning and procurement processes deliver the best service management and delivery arrangements?</p> <p>What measures does the council need in order to effectively challenge performance weaknesses by any providers?</p> <p>How does the council ensure that promised financial and performance benefits are realised and rewarded?</p>	

Source: Audit Commission

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# **Strategic financial management in councils**

## **Good-practice checklist**

Local government, July 2010

# Good-practice checklist

## The checklist

Councillors and senior managers can use this good-practice checklist to examine their financial management arrangements. The checklist is designed to help councillors and senior managers follow the principles of strategic financial management (SFM). It outlines issues to consider and common problems for each of the five characteristics of SFM. The checklist will help councillors and senior managers to identify strengths and weaknesses for their council and identify issues for further investigation and improvement.

This good-practice checklist has been produced to support the Audit Commission's report *Strategic Financial Management in Councils: Delivering Services with a Reduced Income* that is available on the Commission's website at [www.audit-commission.gov.uk/SFM](http://www.audit-commission.gov.uk/SFM)

## Using the checklist

The leadership team could use the checklist to:

- evaluate the council's strengths and weaknesses in financial management;
- improve the discussions on council strategy;
- provide the agenda for a strategy conference;
- introduce a longer-term approach to financial management; or
- support organisational transformation.

The indicators of success could also be translated into actions and objectives for change.

# Adopting strategic financial management – a checklist

Indicators of success	Potential problems
<b>Characteristic one: Strong and accountable financial leadership</b>	
The council leader and the chief executive work together to set the council’s direction.	No agreed long-term vision for the council Lack of support for the corporate direction
The council leader and chief executive are jointly accountable for achievement.	Unclear accountability
The finance director (and elected member with lead responsibility for finance) is part of the leadership team.	The finance director is not part of the leadership team.
There is clear understanding of respective roles, responsibilities and constraints.	Lack of understanding of roles and responsibilities  Little common understanding among officers and members
The leadership team ensures that: <ul style="list-style-type: none"> <li>■ there is regular, productive challenge of financial assumptions and direction;</li> <li>■ there is open and honest discussion about what is desirable and what is affordable;</li> <li>■ responsibility and accountability are clear;</li> <li>■ that information is used to make evidence-based decisions and to manage performance;</li> <li>■ leaders understand the current financial position and potential future opportunities and threats; and</li> <li>■ there is regular, dedicated time for leaders to focus on the strategy.</li> </ul>	The council lacks systems that enable robust and constructive challenge.  Internal disputes or interests undermine attempts to plan  Lack of transparency in decision making  Lack of understanding of the current financial position and potential future implications  A focus on thinking and operating only in the short term
<b>Characteristic two: An organisational culture built on financial awareness</b>	
The council has adopted a transformational approach. Elected members and council staff work together to achieve council goals.	Protectionism of departmental budgets and working practices.
Staff are required and enabled to take collective and individual responsibility for the stewardship of funds and for delivering value for money.	Lack of trust, suspicion and internal disagreement on priorities.
Elected members and council staff trust one another to act responsibly.	
Elected members and council staff are aware of the financial effects of their decisions and actions.	Finance officers work in silos with little regard for wider organisational priorities.

Indicators of success	Potential problems
The leadership team clearly and decisively communicates the long-term financial strategy, the current position, likely challenges and proposed solutions to staff and to external stakeholders.	Poor communication of priorities and challenges.
Staff understand how their roles contribute to the council's priorities.	Officers and members do not know how their roles contribute to the council's priorities.
Staff and elected members are supported to develop financial skills and to understand the principles of financial management.	Financial literacy and knowledge is not rooted in the organisation.
<b>Characteristic three: An ability to specify priorities and make choices within means</b>	
The council leader and chief executive use the strategic priorities and financial position to decide what is practicable in the short, medium and long term.	Departments manage within their own priorities and budgets, without linking to corporate strategy.
The council leader and chief executive consider pressures such as demographic change, economic, environmental, legal and social challenges and future affordability when setting the council's strategic priorities.	No consideration of potential future pressures or challenges
The council leader and chief executive work with the finance director to ensure that resources are allocated to achieve priorities and deliver value for money.	Resource allocation is incremental, based on past budgets and limited performance information.
The strategic priorities drive all council business, from service plans through to the performance objectives of individual staff.	Departments follow individual priorities and keep their own reserves.
Staff use financial strategies and plans to make financial choices and ensure the delivery of strategic priorities.	
The council produces accurate and detailed long-term (ten years or more) financial strategies and medium-term financial plans.	Short-term planning within individual departments
<p>Medium-term financial plans include:</p> <ul style="list-style-type: none"> <li>■ outcome measures;</li> <li>■ scenario plans;</li> <li>■ details of costs and overheads;</li> <li>■ comparative benchmarking information to assess costs and performance;</li> <li>■ links to other relevant council strategies such as workforce plans; and</li> <li>■ details of partnership activities.</li> </ul>	<p>Medium-term financial plans are not reviewed and updated regularly.</p> <p>Realistic scenario planning not present</p> <p>Regular use of reserves to balance budgets</p>

Indicators of success	Potential problems
<b>Characteristic four: Comprehensive financial information clearly underpins decisions</b>	
Elected members and council staff understand why financial information is important.	Officers and members are not prepared to admit knowledge gaps.
Elected members and council staff understand how to use financial information to: <ul style="list-style-type: none"> <li>■ make informed decisions; and</li> <li>■ review past decisions to ensure that expected financial and performance benefits are realised.</li> </ul>	Lack of transparency in decision making
Elected members and council staff use relevant, high-quality information to make decisions.	Decisions are made without considering all relevant information.
Council staff produce information that is comprehensive, timely and easily understood.	Financial resources are not clearly allocated to corporate priorities.
As a minimum, financial information includes details of financial trends, suitable benchmarking information, possible scenarios and their likely impact over the short, medium and long term.	Decisions are based on short-term need, with little or no consideration of long-term consequences.
<b>Characteristic five: An ability to anticipate changing circumstances and manage financial risks</b>	
Financial risk management is an integral part of the council's activities.	All financial risks are given the same attention.
Financial plans include the potential financial impact of corporate and other risks.	Risk registers grow without clear policies on prioritisation or culling.
The council has anticipated and is mitigating the risks arising from reduced funding and increased demand.	The council does not understand the financial implications of its risks.
The council understands the difference between hazard and risk and is risk aware.	The council is risk averse rather than risk aware. Risks and opportunities of alternative service delivery mechanisms are misunderstood.
Opportunities that carry risk are actively managed.	
Scenario plans consider best and worst-case options and cover a wide range of financial and social challenges.	Financial risks are managed in the short term.

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