



National Audit Office

# Financial Management in the Department for Communities and Local Government

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# SUMMARY

**1** This Report examines the financial management of the Department for Communities and Local Government which in 2007-08 was responsible for expenditure of £34,365 million. Financial management is the system by which the resources of an organisation's business are directed and controlled to support the organisation's goals. Good financial management is an essential element of strong corporate governance. It forms part of the firm foundations of an organisation, underpinning service quality and improvement, and is the basis of accountability to stakeholders for the stewardship and use of resources. Effective financial management helps an organisation manage its budgets, allocate resources and make decisions supported by an understanding of the relationship between costs and performance; and deliver its services cost effectively.

**2** The Department's aim is to create vibrant, diverse and attractive places with strong local economies where people want to live, work and raise their families. It takes the lead across government on: housing supply and affordability; local government and services; cohesive communities; regeneration; and emergency planning and the Fire and Rescue Service.

**3** Many of the Department's policies and programmes are delivered through a wide range of local and regional organisations, including local authorities, Regional Development Agencies, Registered Social Landlords, local partnerships and voluntary organisations. The Department also delivers through a number of its own arms length bodies, including the Homes and Communities Agency, the Planning Inspectorate, Urban Development Corporations and the Audit Commission.

**4** The Homes and Communities Agency was formed on 1 December 2008 with the bringing together of English Partnerships, the Housing Corporation's investment programme and a number of the Department's investment programmes. At the same time the recent economic downturn has had a significant impact on the Department's ability to deliver against its objectives in respect of housing supply and regeneration, as both housing associations and private sector developers have faced difficulties in raising the funds necessary to support development. The Department has brought forward funding of some £700 million for the cross-government initiative to support the housing market announced in September 2008. The Department is developing a series of strategic frameworks to help it develop effective responses to these major changes in the external environment.

**5** This report presents the findings and recommendations from our examination of financial management within the Department for Communities and Local Government. Part 1 of this report sets out how the Department is organised and managed. Part 2 analyses the financial performance of the Department and Part 3 presents our detailed assessment of financial management within the Department against the widely accepted five aspects of good financial management.

## Findings

**6 The Department has shown commitment to improving financial leadership and governance, but has more work to do to embed it throughout the organisation.** The Department appointed a Board level Finance Director in September 2006, although this individual's role has since expanded to encompass a range of other corporate services. The Department has also increased the number of non-executive Board members and enhanced its Audit Committee. It has also appointed qualified accountants as Heads of Finance for each of the Departmental Groups. Over the past eighteen months these Heads of Finance have increased their knowledge and expertise so that they are able to exercise increasing influence over key processes and provide an effective challenge function within the Department.

**7 The Department should have more financially trained staff given its size and expenditure.** As of June 2008, some 28 per cent of the Department's finance staff were professionally qualified, compared to an average across public sector organisations of 34 per cent. The Department recognises the need to increase the proportion of financially qualified staff within its finance teams and is making improvements in this area. For example, in its May 2009 reorganisation, the Department's central finance team has increased the proportion of its financially qualified staff to almost 40 per cent. In the wider Department, further recruitment and training of staff with financial and business management skills would allow it to better analyse and interpret financial data and manage complex activities.

**8 The Department has improved its business planning processes and for 2009-10 budgets were agreed before the start of the financial year.** The Spending Reviews determine the Department's overall budget and the spending profile of the major Departmental programmes for the next three years. Financial planning in between Spending Reviews is an annual process generally focussing on managing funding at the margins, such as administration or minor programmes. The Department has made considerable improvements to its annual budgeting process for 2009-10.

**9 The quality and analysis of financial information presented in support of investment decisions is variable.** The Department has established an Investment Board to advise the main Board on new investment decisions. The Board's assessment processes meet the key requirements of the Treasury's Green Book and Office of Government Commerce Gateway Review Approaches to Appraisal. All investment appraisals submitted to the Investment Board contain some financial information, but the level of this information and the degree to which it is analysed, varies. For example, not all business cases contain a sensitivity analysis of the financial data or a compelling body of economic evidence.

**10 The Department's Investment Board processes are not well suited to dealing with situations requiring an urgent response.** The processes are relatively new and still developing, but it can currently take six weeks for proposals to be approved by the Investment Board. Furthermore, to date the Board has conducted very few post- and mid-stage reviews of existing projects, although it is now in the process of developing a programme of project reviews that should help address these issues. The Board is also now considering how it can best respond to urgent business needs.

**11 The Department has made significant improvements to its internal financial monitoring through the development of its Integrated Performance Report.** The Report brings together financial, HR, performance and risk data into one document. This has allowed the non-executive members of the Board to provide a greater level of challenge to the financial information, which has in turn required senior management to acquire a deeper and more complete understanding of the financial information presented.

**12 The Integrated Performance Report has strengthened the Department's risk management process.** This Report provides an opportunity for risks to be highlighted to the Board alongside programme performance and plans. The Department has made a good start to developing its risk management framework, but needs to ensure that it recognises active and regular management of risk as a key element of all jobs in the organisation. The Department is looking to address this through developing bespoke programme and project management training for staff, which will include a focus on active risk management.

**13 The Department does not meet the Treasury's standard to provide in-year reports to the Departmental Board within 10 days of the month end.** The Department considers that it is more important to provide accurate and reliable information, and has developed a timetable that allows sufficient time for effective internal challenge and review, and for consistent commentary to be added.

**14 The Department cannot accurately report expenditure against its Strategic Objectives or other outcome indicators.** The Department can only present notional allocations of financial information by Departmental Strategic Objective, because the expenditure and outcomes of individual programmes may contribute to more than one Departmental Strategic Objective. As a result it cannot easily identify the impact on outcomes of changes in the allocation of resources. The Department recognises the issue, but considers it could only be rectified with major investment that would provide little real benefit for financial decision-making.

**15 The Department has succeeded in producing its annual resource accounts before the Parliamentary Summer Recess every year since 2004-05.** However, the high turnover of staff responsible for preparing the accounts adversely affected both the timing and quality of the 2007-08 accounts. The Department aspires to publish its Annual Report and its annual resource accounts in a single document in the future.

## Overall Financial Management Conclusion

**16** The Department is committed to good financial management at senior management and Board level and has introduced processes to improve its financial management systems and the financial capability of its staff. The Department does still have more to do to embed good financial management throughout the organisation, which is made more challenging by the complex delivery framework within which it operates.

## Recommendations

- 17** We recommend the following actions:
- a** **The Department still needs to fully assess where it has gaps in its financial and business management skills and bring in new expertise where appropriate.** It needs to build on its existing actions to enhance financial and business management capacity across the organisation, including its intention both to launch a Learning and Development Framework in Summer 2009 to improve arrangements for financial and resource management training, and to increase the proportion of professionally qualified finance staff. We consider that Board level financial challenge would be more effective if delivered by an executive member whose responsibilities were solely or mainly concerned with financial management.
  - b** **The work of the Department's Investment Board is valuable, but could be further developed and improved.** We welcome the Department's intention to develop a fast-track process to consider urgent cases, enhance the consistency of financial analysis by setting minimum information requirements, and develop a process for conducting more post- and mid-stage reviews of existing projects.
  - c** **The Department does not fully understand the linkages between costs and performance as measured by its Public Service Agreements and Departmental Strategic Objectives.** While accepting the Department's reluctance to invest in a major new costing system, it should consider how it might better develop the relationship between funding and performance measures, so that it improves its understanding of the impact of funding decisions on performance and outcomes.

- d** The majority of the Department's expenditure is fixed funding allocated to delivery partners and is therefore relatively straightforward to forecast. Line managers' forecasting of more volatile expenditure is less accurate, although in recent years the Department has consistently reported an annual expenditure outturn that is within budget. The Department should explicitly assess the quality of line managers' forecasting, business and financial management as part of their performance appraisal, in order to encourage improvements in the accuracy of forecasts in future years.
- e** The Department does not yet meet the Treasury's standard to provide in-year reports to the Departmental Board within 10 days of the month end. As the new reporting system beds in, the Department should aim to reduce the time taken to deliver the Integrated Performance Report to the Board. The Department should also encourage senior managers to access the underlying electronic information as soon as it is available to ensure that they have an up to date understanding of the business performance.
- f** The Department has made a good start to developing its risk management framework and has risk registers in place, but needs to encourage all staff to understand how active risk management can be used to enhance business performance and to make it a key element of all jobs. The Department is looking to encourage this process by developing bespoke programme and project management training for staff, as well as by promoting the importance of the half yearly Directors' assurance statements and linking them to an active review of the quality of Divisional risk registers.