



National Audit Office

**REPORT BY THE
COMPTROLLER AND
AUDITOR GENERAL**

**HC 187
SESSION 2010–2011**

6 JULY 2010

Ministry of Justice

Financial Management Report

Our vision is to help the nation spend wisely.

We apply the unique perspective of public audit to help Parliament and government drive lasting improvement in public services.

The National Audit Office scrutinises public spending on behalf of Parliament. The Comptroller and Auditor General, Amyas Morse, is an Officer of the House of Commons. He is the head of the National Audit Office which employs some 900 staff. He and the National Audit Office are totally independent of Government. He certifies the accounts of all Government departments and a wide range of other public sector bodies; and he has statutory authority to report to Parliament on the economy, efficiency and effectiveness with which departments and other bodies have used their resources. Our work leads to savings and other efficiency gains worth many millions of pounds: £890 million in 2009-10.



National Audit Office

Ministry of Justice

Financial Management Report

Ordered by the House of Commons
to be printed on 5 July 2010

Report by the Comptroller and Auditor General

HC 187 Session 2010–2011
6 July 2010

London: The Stationery Office
£14.75

This report has been
prepared under Section 6
of the National Audit Act
1983 for presentation to
the House of Commons
in accordance with
Section 9 of the Act.

Amyas Morse
Comptroller and
Auditor General

National Audit Office

2 July 2010

This report examines the financial management of the Ministry of Justice, which in 2008-09 was responsible for some £10.1 billion of expenditure, employed some 95,000 staff and delivered justice services to nine million people across the United Kingdom.

© National Audit Office 2010

The text of this document may be reproduced free of charge in any format or medium providing that it is reproduced accurately and not in a misleading context.

The material must be acknowledged as National Audit Office copyright and the document title specified. Where third party material has been identified, permission from the respective copyright holder must be sought.

Printed in the UK for the Stationery Office Limited
on behalf of the Controller of Her Majesty's Stationery Office
2375843 07/10 STG

Contents

Summary **4**

Part One

How the Ministry is organised
and managed **10**

Part Two

Financial performance in the
Ministry of Justice **16**

Part Three

Financial management in the
Ministry of Justice **24**

Appendix One

Methodology **35**

The National Audit Office study team
consisted of:

Nick Bateson, Elisabeth Thornton,
Paul Mills, Rebecca Bentall-Lynch and
Paul Bishop, under the direction of
Paul Keane

This report can be found on the
National Audit Office website at
[www.nao.org.uk/moj-financial-
management-2010](http://www.nao.org.uk/moj-financial-
management-2010)

For further information about the
National Audit Office please contact:

National Audit Office
Press Office
157-197 Buckingham Palace Road
Victoria
London
SW1W 9SP

Tel: 020 7798 7400

Email: enquiries@nao.gsi.gov.uk

Summary

1 This report examines the financial management of the Ministry of Justice (the Ministry), which in 2008-09 was responsible for some £10.1 billion of expenditure and administered £37 billion of grant payments to the Scottish and Welsh devolved administrations.

2 The Ministry was established in May 2007, through combining the criminal justice elements of the Home Office with the Department for Constitutional Affairs. The Ministry is made up of a small corporate and policymaking centre and a range of delivery bodies that constitute some 94 per cent of its expenditure. Since its inception, the Ministry has been subject to significant machinery of government changes, including the establishment of the National Offender Management Service agency in April 2008, which represented some 49 per cent of the Ministry's overall expenditure in 2008-09.

3 Effective financial management is crucial to strong corporate governance, ensuring an organisation's resources are directed and controlled to support its aims and objectives. It forms part of the foundations of an organisation, underpinning service quality and improvement and is the basis of accountability to stakeholders for the stewardship of its assets and use of resources.

4 The Ministry has wide ranging responsibilities across the justice sector and a nationally important remit, encompassing the courts, prisons and probation services. To deliver this remit, the Ministry has a range of interlinked arm's length bodies and delivery chains. In addition, the Ministry is operating under considerable financial pressure, due to the current spending environment. Strong, consistent and flexible financial management processes are, therefore, crucial in ensuring that these arm's length bodies are held to account and that the Ministry is able to monitor its financial and operational risks effectively, respond to problems quickly and deliver improvements in services within the constraints of available resources. This is particularly important following the recent Budget announcements.

5 This report presents the findings and recommendations from our examination of the Ministry's financial management in three parts:

- Part One – how the Ministry is organised and managed;
- Part Two – the financial performance of the Ministry; and
- Part Three – our assessment of financial management within the Ministry.

6 During our fieldwork for this study in late 2009, we met with the Ministry's senior executives and examined evidence underpinning the Ministry's financial management systems and 2008-09 reported performance, to conclude on its effectiveness.

7 The Ministry has a diverse structure, a nationally important delivery portfolio and a significant operational budget. In addition, the Ministry needs to ensure that it can deliver sustainable cost reductions to meet the demanding targets outlined in the recent Budget. To manage these challenges, the Ministry needs effective strategic and operational financial management capacity, supported by consistent integrated financial and operational management information and good quality financial reporting. We found that the Ministry is making progress in improving in its financial management. It has identified the main financial management challenges it is facing and has begun to address them. However, we have identified the following areas of weaknesses:

- the consistency of the Ministry's financial management approach;
- the Ministry's understanding of its costs;
- consolidation of the Ministry's financial management systems and processes; and
- the delivery of the Ministry's financial management improvement initiatives.

8 Our key findings in these areas are outlined below.

Key findings

The consistency of the Ministry's financial management approach

9 The Ministry has complex delivery mechanisms and accountability structures in its executive agencies. This makes it difficult for the Ministry to introduce consistent financial management processes, reducing their efficiency and increasing their cost. The Ministry has a range of financial management processes and accountability structures in its executive agencies, who are primarily responsible for delivering its challenging remit. The Ministry has yet to consolidate these processes, particularly in the National Offender Management Service, its largest executive agency, whose financial management has yet to be integrated with the Ministry's.

10 The Ministry's financial management and monitoring processes did not identify the emerging control issues in the Legal Services Commission, its largest Non-Departmental Public Body, in time for the Ministry's Board to address them and prevent their accounts being qualified. The Ministry and the Legal Services Commission have begun to address these control issues. In addition, the Ministry has announced its intention to convert the Legal Services Commission from a Non-Departmental Public Body to an executive agency. The Ministry's monitoring systems did not enable the Board to intervene in the Legal Services Commission's control environment quickly enough to enable its emerging control issues to be addressed.

The Ministry's understanding of its costs

11 The Ministry does not understand the costs of its activities within prisons, the probation service, and the courts in sufficient detail. This reduces the Ministry's ability to allocate resources on the basis of relative financial and operational performance of individual prisons, probation services and courts.

The Ministry has improved its understanding and control of the costs of its external goods and services by enhancing its procurement function. However, some 40 per cent of the Ministry's cost base relates to staff time. The Ministry has introduced two major costing programmes, Specification Benchmarking and Costing in the National Offender Management Service, and activity-based costing in HM Courts Service to improve its knowledge of its staff-based costs. These have the potential to generate significant savings and operational benefits, but the overall programme is not due to be completed until March 2012.

12 The Ministry's Finance Directorate does not have sufficient visibility of the costs of policy proposals, affecting its ability to monitor their financial implications centrally.

The Ministry has recognised the importance of producing fully costed policy initiatives and is improving the coordination of its policy proposals through its Policy Committee and economists embedded in local policy areas.

The Ministry's financial management systems and processes

13 The Ministry's multiple financial data systems impact on the Board's ability to monitor its overall budgetary position, emerging financial risks and staff numbers.

Due to machinery of government changes, the Ministry has been subject to significant revisions to its structure since it was established. This has resulted in a legacy of multiple data systems, which reduces the Board's ability to monitor its financial position; ensure the timely flow of financial and operation information; produce accurate month-end reports and monitor financial risks as they develop.

14 The Ministry currently does not produce combined financial and operating reports for the Board, and its financial reports include information on expenditure and income only. This reduces the Board's ability to monitor the Ministry's full range of assets, liabilities and future cash requirements.

The Ministry produces operational reports highlighting performance against its Departmental Strategic Objectives, which include information on the progress of major programmes. However, these reports are not integrated with the Ministry's financial reporting and the Board's financial reports do not include information on its balance sheet and cash flow position.

Delivery of the Ministry's financial management improvement initiatives

15 The Ministry has recently drawn together its financial management improvement projects. However, it is yet to define the importance of financial management in its future development or deliver its programme of improvements.

The Ministry's Board has made good progress in improving its financial management. It has identified that it needs to integrate its financial systems, deliver its future efficiency programme and improve its internal financial reporting. The Ministry has also introduced its Value for Money Improvement Committee to develop and oversee its financial plans and monitor their delivery. However, the Ministry is yet to commit to a clear, comprehensive action plan to deliver the projects within its financial management improvement programme.

16 The Ministry's Performance and Efficiency Programme has been effective in providing a clear direction for efficiency across its corporate centre and arm's length bodies. The Performance and Efficiency Programme has encouraged staff to engage in the process of delivering efficiency savings and, through this programme, the Ministry has started to spread existing effective operational practice. This focus has also helped the Ministry to live within its budget in recent years despite increasing cost pressures in courts, prisons and probation. The Ministry has reported that it is on track to delivery £1 billion of savings during the current Government Spending Review period. The Ministry will face further efficiency challenges in the coming Government Spending Review, to be completed in autumn of this year, but it is beginning to plan for the delivery of these efficiencies, building on the disciplines it established in the Performance and Efficiency Programme.

Overall Conclusion

17 The Ministry has recognised the need to improve its financial management. The Ministry has also introduced programmes to better understand its costs and integrate its financial systems, for example, by establishing its Value for Money Improvement Committee and enhancing its procurement function. The National Audit Office welcomes these initiatives, however, we view the Ministry's present financial management as below best practice in three significant areas:

- **The consistency of the Ministry's financial management approach.** The Ministry's differing financial management processes in its arm's length bodies reduce the efficiency of its financial management and affect the Board's ability to monitor its full range of financial and operational risks.
- **The Ministry's understanding of its costs.** The Ministry's incomplete knowledge of the costs of its activities and policy proposals reduces its ability to make decisions on the efficient allocation of resources.
- **The Ministry's financial management systems and processes.** The Ministry's multiple financial systems and incomplete financial reports affect the Board's ability to monitor its overall budgetary position and awareness of the full range of the Ministry's assets, liabilities and future cash requirements.

18 In the light of these findings, the National Audit Office believe there is a pressing need to ensure that the Ministry's financial management improvement programmes are delivered through a coherent, controlled and measurable change programme. We believe that this programme should be put in place within the next four months to ensure that the Ministry focuses on the delivery of its financial management initiatives and demonstrates its commitment to further improving its financial management.

Recommendations

19 The National Audit Office makes the following recommendations:

Delivery of the Ministry's financial management improvement initiatives

a **The Ministry has yet to commit to a clear plan for the delivery of its financial management improvement initiatives.** The Ministry should, within the next four months, articulate a strategy for the development of financial management across its span of control and set clear milestones and resource requirements for the delivery of its programme of financial management improvements.

The consistency of the Ministry's financial management approach

b **The Ministry's accountability structures and delivery model affects its ability to introduce consistent financial systems and processes across its remit and ensure the timely flow of financial and operational information.** In its review of its arm's length bodies, the Ministry should seek to streamline its financial systems and accountability structures to facilitate the introduction of consistent financial management processes.

c **The Ministry's financial management systems did not bring the control weaknesses within the Legal Services Commission to the Board's attention in time.** To improve its control framework for its Non-Departmental Public Bodies and ensure the Accounting Officer is able to gain sufficient assurance over their financial and operational risks, the Ministry should:

- clarify its monitoring remit with its Non-Departmental Public Bodies;
- determine the circumstances in which it would intervene to strengthen their control environment; and
- clarify the role of its Internal Audit function in relation to its arm's length bodies.

The Ministry's understanding of its costs

- d** **The Ministry does not understand the detailed costs of the delivery of its activities across its full range of arm's length bodies and activities.** To drive long term and sustainable efficiencies, and to enable it to make informed decisions on relative operational performance, the Ministry should, where resources permit, look to accelerate its Specification, Benchmarking and Costing programme in the National Offender Management Service, and activity-based costing work in HM Courts Service. It should also plan how it will use the outputs from these programmes to drive cost savings and should seek to expand these programmes to the Ministry's other delivery bodies.

- e** **The Ministry's Finance Directorate does not have sufficient visibility of the costs of its proposed policy initiatives reducing its ability to manage its forward policy programme within the constraints of its available resources.** The Ministry's Finance Directorate takes assurance from its Policy Committee and economists embedded in local policy areas for the costs of proposed policy. However, the Ministry should ensure that its Finance Directorate is able to monitor the likely costs of policy proposals centrally.

The Ministry's financial management systems and processes

- f** **The Ministry does not produce integrated operational and financial reports affecting the Board's ability to make decisions on the basis of the full range of relevant performance information.** The Ministry should build on the recent improvements it has made to its financial monitoring processes by:
 - producing a combined report for the Board including: all relevant financial information (covering income and expenditure, financial commitments, assets, liabilities, cash flows and staff numbers); operational performance and risk data; and
 - providing a clear commentary in the report describing the data, the potential implications and the decisions that are required by the Board.

Part One

How the Ministry is organised and managed

1.1 The Ministry of Justice (the Ministry) was formed in May 2007, through combining the criminal justice elements of the Home Office with the Department for Constitutional Affairs (DCA). This put responsibility for the whole justice system in one department for the first time. In a further major restructure, the National Offender Management Service was created in April 2008, by merging HM Prison Service, the National Probation Service and their headquarters functions, which had previously been located within the Ministry.

1.2 The Ministry's purpose is to create a safe, just and democratic society and it is responsible for criminal justice policy, courts, prisons and probation services. It also leads the Government's constitutional, rights and legal reform programmes. The Ministry's resource requirement is some £47.1 billion, although £37 billion represents funding for the devolved Scottish and Welsh Governments¹. The remaining £10.1 billion represents the costs of the Ministry's primary activities. The Ministry employs more than 95,000 staff and each year provides services directly to around nine million people across the United Kingdom. **Figure 1** shows the Ministry's network of arm's length bodies and the split of the its costs and cash flows between them.

Objectives

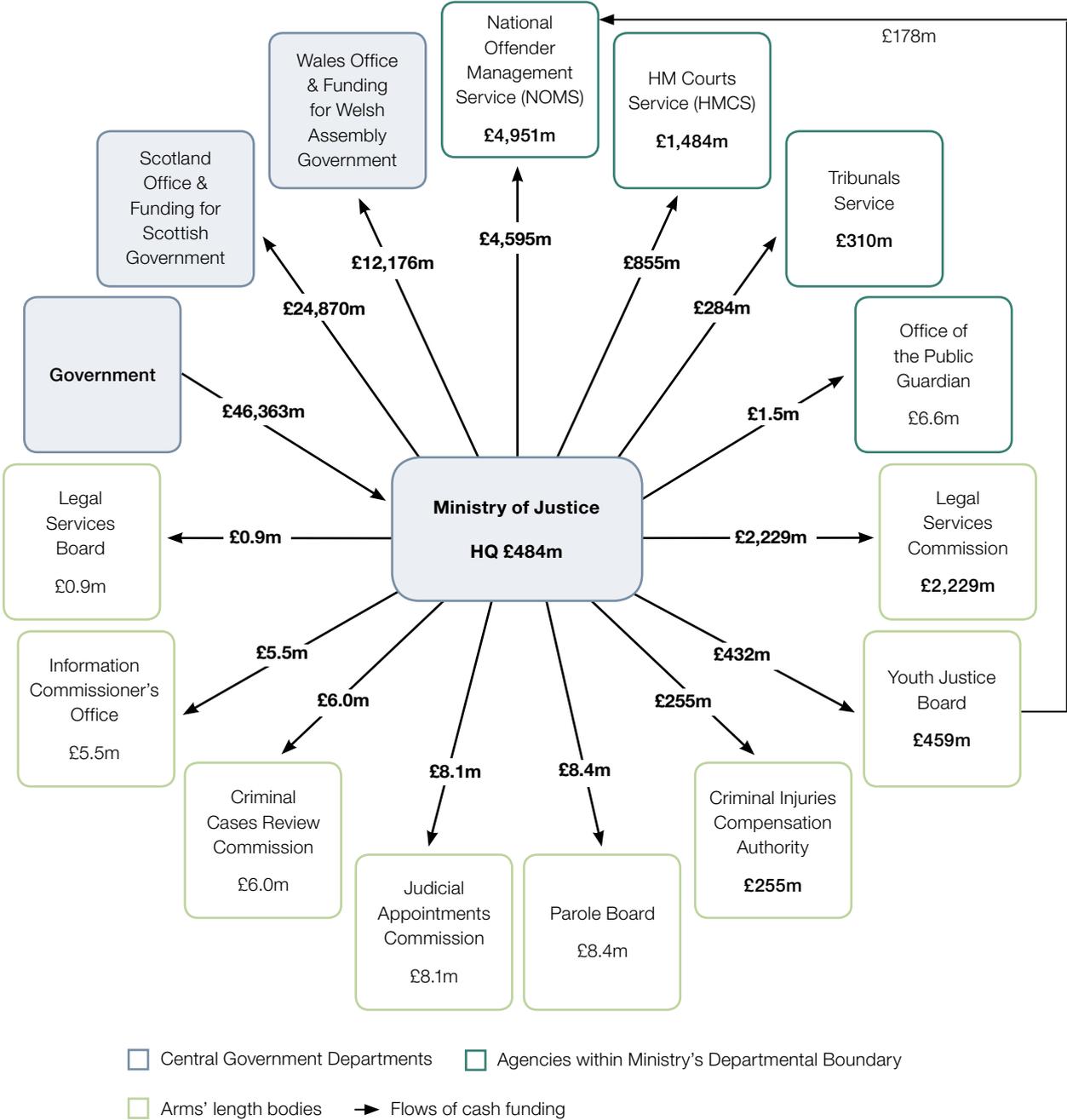
1.3 The Ministry has four Departmental Strategic Objectives (DSOs):

- Strengthening democracy, rights and responsibilities.
- Delivering fair and simple routes to civil and family justice.
- Protecting the public and reducing re-offending.
- A more effective, transparent and responsive criminal justice system for victims and the public.

1.4 In addition, the Ministry is the lead department for Public Service Agreement (PSA) 24: to deliver a more effective, transparent and responsive criminal justice system for victims and the public, and contributes to nine other PSAs which are led by other government departments.

¹ Due to the devolved nature of these functions, these grants, and the services that relate to them, are outside of the scope of this report.

Figure 1
The Ministry’s network of arm’s length bodies, showing cash flows and use of resources



NOTE

1 The Ministry contains several other small independent bodies, such as HM Inspectorate of Prisons, which are funded within the Ministry's central and administrative funding of £661m.

Source: Cash flows and resource requirements from the Ministry of Justice and other entities' accounts 2008-09

Organisation and delivery

The Core Ministry is responsible for policy, funding and regulation

1.5 The Core Ministry comprises the Ministry's headquarters and the administrative functions of the Wales Office and the Scotland Office. The Ministry's headquarters supports Ministers in policy, funding and regulation and is organised into five Business Groups, aligned to the Ministry's DSOs, as detailed in **Figure 2**. Four of the five Business Groups (Democracy, Constitution and Law; Access to Justice; National Offender Management Service; and Criminal Justice) are responsible for delivery, while the Corporate Performance Group provides strategic input and support functions.

1.6 The Ministry also hosts the Office for Criminal Justice Reform. The Office for Criminal Justice Reform works with the Home Office and the Attorney General's Office to support all criminal justice agencies in their role of providing an improved service to the public and is accountable to three respective Ministers.

The Ministry has a range of delivery bodies who are responsible for 94 per cent of its expenditure

1.7 The Ministry is reliant on its executive agencies, Non-Departmental Public Bodies (NDPBs) and other sponsored bodies to provide services to the public. In 2008-09, 94 per cent of its expenditure was spent on its behalf by its sponsored bodies. The responsibilities of the Ministry's largest delivery bodies are detailed below.²

Executive Agencies

National Offender Management Service

Responsible for correctional services in England and Wales, through the prison and probation systems.

HM Courts Service

Responsible for the courts system in England and Wales.

Tribunals Service

Provides common administrative support to central government tribunals.

Office of the Public Guardian

Supports and promotes decision-making for those who lack the capacity to make decisions for themselves.

Major Non-Departmental Public Bodies

Legal Services Commission

Runs the legal aid scheme in England and Wales.

Youth Justice Board

Oversees the youth justice system in England and Wales.

Criminal Injuries Compensation Authority

Administers the Criminal Injuries Compensation Scheme in England, Scotland and Wales.

² On 3 February 2010, the Justice Secretary announced that the Legal Services Commission would be converted from a Non-Departmental Public Body to an executive agency. On 24 March 2010, the Ministry announced that HM Courts Service and the Tribunals Service would be merged into a new executive agency.

Figure 2
The Ministry's delivery network

	Corporate Performance	National Offender Management Service	Access to Justice	Criminal Justice (Includes Office for Criminal Justice Reform)	Democracy, Constitution & Law	Wales Office	Scotland Office
Ministry Core							
Ministry HQ Business Group							
Total Ministry Group expenditure	£484m	£4,973m	£4,546m	£618m	£71m	£12,176m	£24,870m
Responsible for	Corporate strategy and professional services	Delivery of adult offender management	Delivery of justice system	Criminal justice and offender management strategy	Policy on constitutional rights and legal reform	Represents Welsh interests within the UK Government	Represents Scottish interests within the UK Government
Departmental Strategic Objective	N/A	Protecting the public and reducing re-offending	Delivering fair and simple routes to civil and family justice	A more effective, transparent and responsive criminal justice system for victims and the public	Strengthening democracy, rights and responsibilities		
Ministry consolidation							
Executive Agencies	N/A	NOMS Agency	HM Courts Service Tribunals Service Office of the Public Guardian	N/A	N/A		
Outside Ministry accounting boundary							
Arm's length bodies	N/A	Probation Boards and Trusts	Criminal Injuries Compensation Authority Legal Services Commission Judicial Appointments Commission Parole Board Criminal Case Review Commission Legal Services Board	Youth Justice Board	Information Commissioner's Office Law Commission		

Source: Ministry of Justice Resource Accounts 2008-09

1.8 Through this delegated structure, the Ministry's responsibilities are administered through long delivery chains, particularly in HM Courts Service and the National Offender Management Service, as illustrated in **Figure 3**. This presents the Ministry with a significant challenge in standardising its financial management processes and ensuring the accurate and timely flow of financial and operational information.

1.9 The Ministry has sponsor units responsible for the general oversight of each NDPB. This includes agreeing the NDPB's framework and the respective management and financial responsibilities of the NDPB and the Ministry.

Accountability and governance

1.10 As Principal Accounting Officer, the Ministry's Permanent Secretary is accountable for its performance, organisation and delivery, as well as the propriety and regularity of its expenditure. He is supported in this role by the Board, which comprises the Directors General of each Business Group; the Director General Finance; the Director General Transforming Justice; and two non-executive directors. The Board sets the Ministry's vision and strategy, manages departmental performance and allocates resources.

1.11 The Ministry also has six committees that support the Board on the following cross-cutting themes as outlined in the box below.

Board sub-committees

Policy

Identifies and sets the strategic policy direction of the Ministry.

Value for Money Improvement Committee

Develops the Ministry's financial plans for the Board and Ministers; and oversees delivery of these plans to ensure the Ministry lives within its resource allocations and meets its value for money targets. The Ministry's Investment Committee and Procurement Committee report to the Value for Money Improvement Committee.

Transforming Justice Committee

Oversees the Ministry's transformation agenda, mission critical programmes and people, IT, finance and commercial strategies.

Corporate Audit

Advises the Permanent Secretary on the Ministry's risk management, control and corporate governance processes, internal and external audit activities and the Ministry's Resource Accounts.

Information

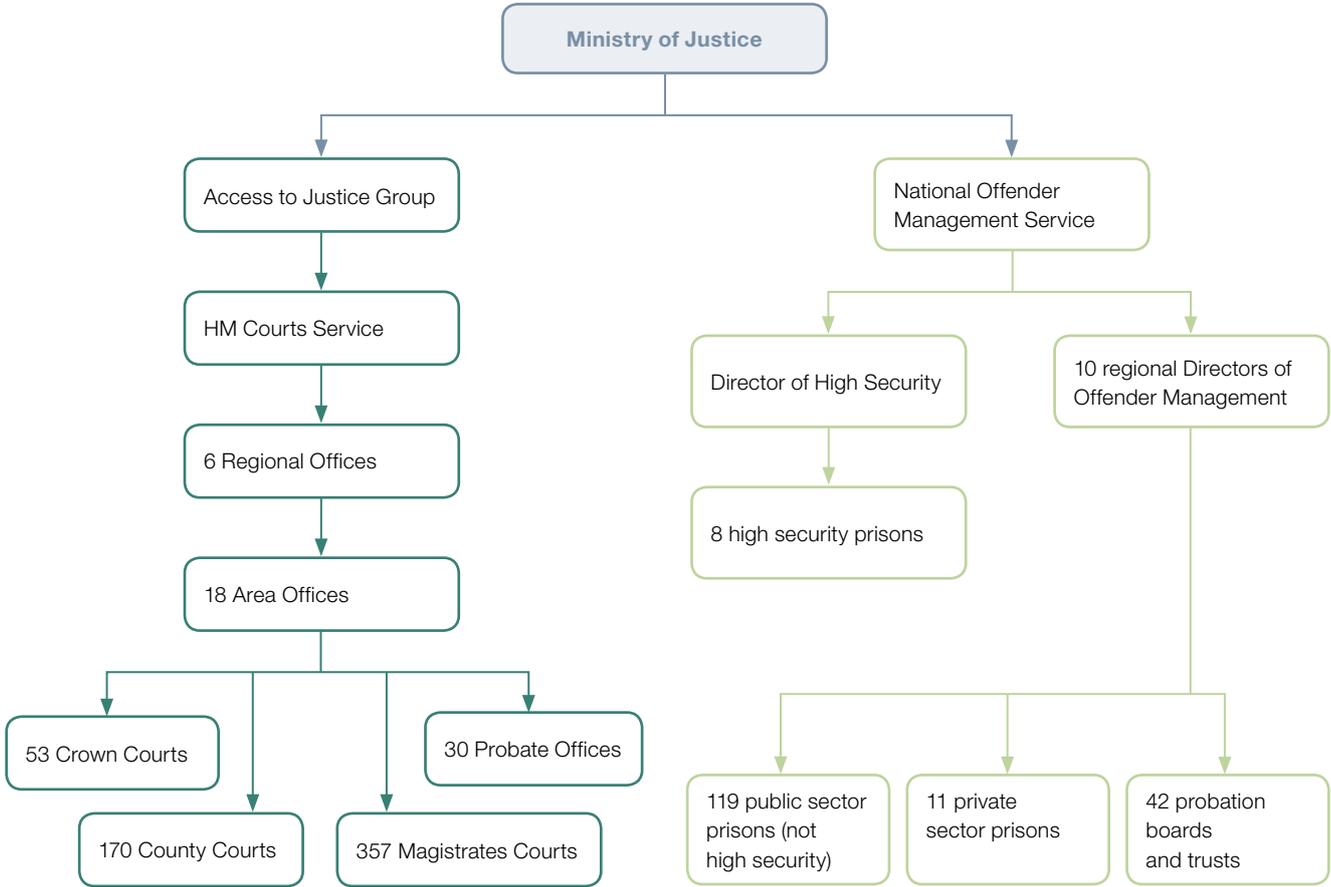
Provides board level accountability for the handling of information and enables the Ministry's Senior Information Risk Officer to fulfil her responsibilities.

Honours

Endorses OBE and MBE recommendations and considers awards above OBE.

Source: Ministry of Justice

Figure 3
 Delivery chains in HM Courts Service¹ and the National Offender Management Service



NOTE
 1 In addition to its 6 regional offices, HM Courts Service has two further offices overseeing Wales and the Royal Courts of Justice Group. Following a recent restructuring within the Ministry, HM Courts Service’s finance function now reports directly to the Ministry rather than through the Access to Justice Group.

Source: National Audit Office analysis of the Ministry’s management structures

Part Two

Financial performance in the Ministry of Justice

Introduction

2.1 The financial performance of the Ministry impacts upon taxpayers, its partners and suppliers through its use of resources to deliver its core objective of developing a modern, fair, cost-effective and efficient system of justice. The Ministry has to manage its finances in accordance with the authority and limits delegated to it by Parliament and budgetary control imposed by HM Treasury.

Management of financial resources

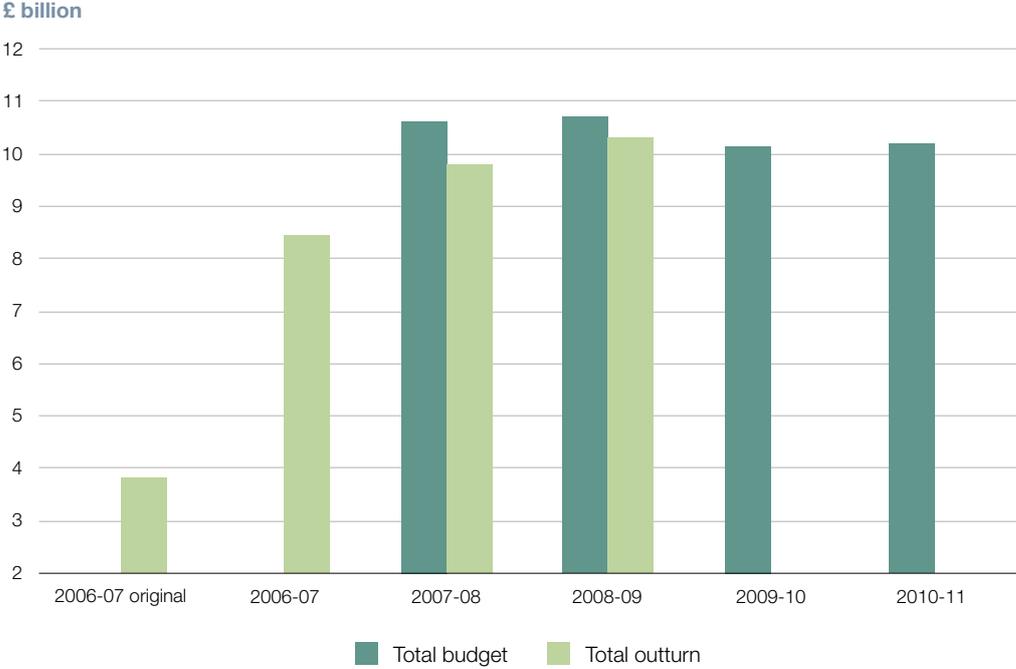
2.2 The Ministry's 2008-09 expenditure was £10.1 billion. The budgeted and actual expenditure of the Ministry is significantly greater than its predecessor body, the Department for Constitutional Affairs (DCA), following the machinery of government change in 2006-07 which greatly increased its size and responsibilities (**Figure 4**).

2.3 In 2008-09, the Ministry underspent its resource budget by £369 million (3.7 per cent), above the average of 2.5 per cent across the major government departments between 2003-04 and 2008-09.³ Historically, the Ministry has not managed to spend its entire budget, particularly capital, although capital underspends have been on a downward trend, as shown in **Figure 5**.

2.4 The proportion of resource budget underspent by the Ministry has been less than 5 per cent of the Ministry's estimate in recent years. However, at the level of individual business areas, there were significant differences between the forecast at the end of February and outturn at the end of March 2009, and a mix of under and overspends for 2008-09, as shown in **Figure 6** on page 18. This shows that the Ministry was not able to forecast its year-end outturn accurately in February, with variances between forecast and outturn of 18 per cent in its headquarters, 15 per cent in HM Courts Service, 3 per cent in the National Offender Management Service and 9 per cent in Probation Services. The 15 per cent variance in HM Courts Service between forecast and outturn is mainly due to year-end changes in asset values of £175 million.

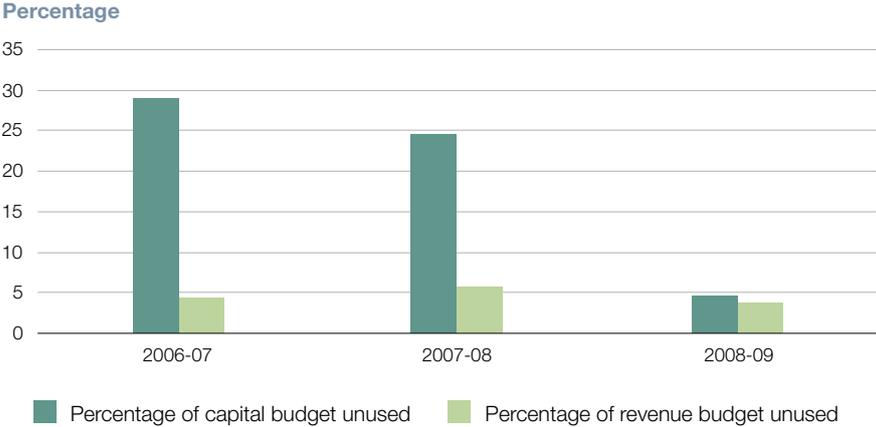
³ Sources: Ministry's Resource Accounts and NAO analysis of departments' Resource Accounts.

Figure 4
The Ministry's historical resource budgets and spending



Source: National Audit Office analysis of the Ministry of Justice's Resource Accounts

Figure 5
The Ministry has consistently underspent against its budgets



Source: National Audit Office analysis of Ministry of Justice Resource Accounts

Figure 6The Ministry's performance against its budget in 2008-09¹

	Estimate	Period 11 forecast (near and non-cash)	Year-end outturn	Underspend/ (overspend) against forecast		Underspend/ (overspend) against Estimate	
	£m	£m	£m	£m	%	£m	%
HQ + rest of Ministry	4,108	3,335	3,924	(589)	(18)	184	4
HM Courts Service	1,322	1,408	1,190	218	15	132	10
NOMS agency	4,023	4,039	4,162	(123)	(3)	(139)	(3)
Probation Boards and Trusts	895	867	787	80	9	108	12
NOMS agency total	4,918	4,916	4,949	(43)	(1)	(31)	(1)

NOTE

1 The forecast figures are the total of the Ministry's near cash and non-cash forecast in its February 2009 management accounts. The estimate and outturn figures are taken from Note 2 of the Ministry's 2008-09 Resource Accounts. Due to differences in the approach to funding of Probation Trusts, their costs are reported against the NOMS Agency line in the table. The Ministry did not revise their Estimate in year for this transfer.

Source: National Audit Office analysis of the Ministry's management accounts and 2008-09 Resource Accounts.

2.5 At the year end the Ministry had revenue underspends in its headquarters (4 per cent), HM Courts Service (10 per cent) and Probation Services (12 per cent); and an overspend in the National Offender Management Service (3 per cent). The variance of £108 million between estimate and outturn for Probation Boards and Trusts is due to the Ministry setting their initial Estimate on the basis of the costs of 42 Probation Boards being reflected in the Probation Boards and Trusts line. Six Boards, costing some £116m, achieved Trust status during the year.

2.6 Since 2008-09, the Ministry has improved its forecasting and budgetary management procedures. As a result, at February 2010, the Ministry was forecasting that its near and non-cash outturn would be within 1 per cent of its 2009-10 estimate.

The Ministry's management of its revenue expenditure

2.7 The Ministry's administration costs have reduced over the last three years, from £575 million in 2006-07 to £433 million in 2008-09, largely due to reallocation of costs between administration and programme expenditure. The Ministry has committed to reduce its overall expenditure by 3 per cent in real terms during both 2009-10 and 2010-11, with the aim of delivering £1.077 billion of annual efficiency savings by the end of the 2007 Spending Review Period in 2011.

2.8 As part of HM Treasury's cross-government Operational Efficiency Programme, the Ministry has gathered standardised data on its back office support costs across the business to enable them to be benchmarked (**Figure 7**).

2.9 HM Treasury's recently published benchmarking exercise of central government back office functions⁴ showed that the relative costs of the Ministry's functions as a proportion of organisational running costs, are below the average across government.

The Ministry's capital underspend is partly due to the prison capacity programme

2.10 During 2008-09, the Ministry's total capital expenditure was £909 million. The National Offender Management Service spent £553 million against a budget of £586 million in 2008-09, an underspend of 5.6 per cent. Around 80 per cent⁵ of this expenditure related to the complex £1.2 billion prison capacity programme,⁶ which is being delivered through a mixture of both public prisons and privately built and run prisons. The capital underspend in 2008-09 was partly due to the timing of approval of the costs of the Ministry's prison capacity programme.

The Ministry's cash balance has increased in recent years

2.11 The Ministry is holding increasing levels of cash (**Figure 8** overleaf). At the end of the 2008-09 financial year, it held £449 million, a £200 million increase since 31 March 2007. As described in Part Three of the report, the Ministry does not currently monitor its cash flow position at Board level.

Figure 7
The Ministry's back office costs and indicators for 2008-09¹

Indicator	Finance	HR	IT	Procurement
Total cost of the function ²	£73.2m	£108m	£252m	£20m
Cost as proportion of total Ministry running costs expenditure ³	1.1%	1.6%	3.7%	0.3%
Operational Efficiency Programme averages ⁴	1.4%	1.8%	7.4%	0.5%

NOTES

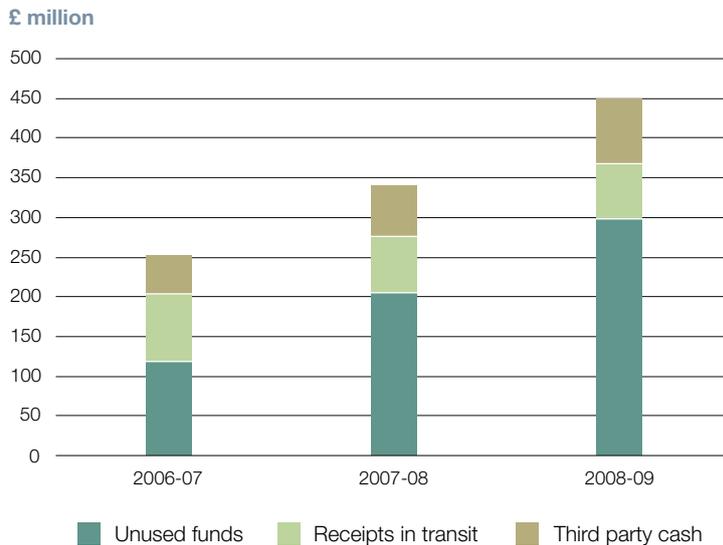
- 1 These combined figures are for the central Ministry and its executive agencies. They do not include its NDPBs which are outside the departmental boundary.
- 2 This includes the cost of out-sourced activities.
- 3 Costs for IT relate to 'run and maintain' IT expenditure and not capital enhancements.
- 4 HM Treasury's Operational Efficiency Programme (Median figures for Finance and HR, Mean figures for IT and Procurement).

Source: National Audit Office analysis of Ministry of Justice data

- 4 HM Government – *Benchmarking the Back Office: Central Government*, HM Treasury Publication Unit, 2009
- 5 Estimate based on NOMS's January 2009 management accounts figures.
- 6 Announced by the Justice Secretary on 5 December 2007. This programme aims to increase prison capacity from 85,000 places at April 2009 to 96,000 places by 2014.

Figure 8

The Ministry is holding increased amounts of cash



Source: National Audit Office analysis of Ministry of Justice Resource Accounts

2.12 One of the key factors in managing government cash efficiently and effectively is keeping as much money at the Exchequer as possible so that publicly available funds can be used efficiently across the whole of government.⁷ The Ministry has increased the proportion of cash balances which it holds in the Government Banking Service, rather than in commercial banks, from 73 per cent in 2006-07 to 94 per cent in 2008-09. This reflects the Ministry's response to HM Treasury's increased focus on cash management in recent years and its drive to reduce the level of cash held outside of the Government Banking Service.

The Ministry is not recovering all of its costs via fee income

2.13 The Ministry recorded income totalling some £1 billion in 2008-09. Forty four per cent of this (£477 million)⁸ came through HM Courts Service as fees for Civil and Family Court work. HM Treasury guidance advises that fees should be set to recover the full cost incurred. For court fees, exemptions and remissions are provided under statute to ensure that access to justice is not restricted, meaning that HM Courts Service has a target of achieving full cost recovery after taking into account exemptions and remissions.

⁷ Report by the Comptroller and Auditor General, *Government cash management* (HC 456 2008-09).

⁸ Source: 2008-09 Resource Accounts

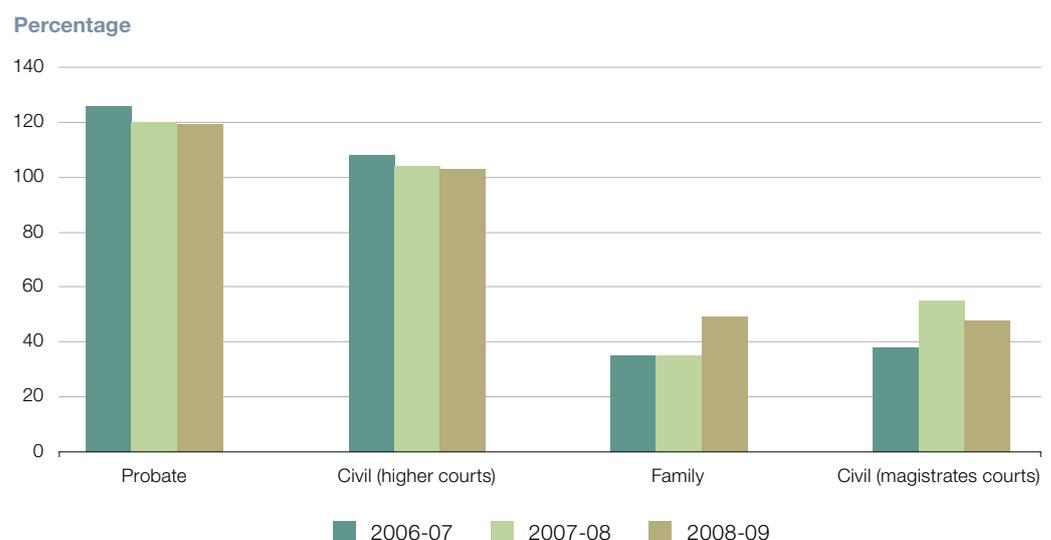
2.14 In 2008-09, the fees received for Civil and Family Court work amounted to only 82 per cent of the cost after taking account of exemptions and remissions, with shortfalls principally in Family Court and Magistrates' Court Civil business, which together represent about a quarter of the fee income and where recovery rates have been historically low. HM Courts Service has made steady progress in moving towards its target for all categories (**Figure 9**), with the latest fee increases for family and civil cases introduced in July 2009. However, due to the current economic environment, the level of recovery is likely to decline in 2009-10.

2.15 There are limitations in the ability of HM Courts Service to predict fee income accurately, as it is reliant on a variety of different information streams to collect data on volumes and income by fee type. HM Courts Service is seeking to incorporate data on the response of its customers to changes in fees.

2.16 HM Courts Service is looking to improve the quality of its customer and management information to improve its ability to predict court fee income by working with the bulk issuers of fees such as banks, water companies and local authorities. However, its ability to monitor the impacts of changes to its fees is affected by the number of people who are exposed to the system infrequently, in many cases only once, from whom it is difficult to gain meaningful data. Overall, although achieving full cost recovery for fees after taking account of exemptions and remissions is difficult, the Ministry needs to do more to model the impact of changes in its fee structures on its customers, to improve its ability to set optimum fees to achieve its target.

Figure 9

Recovery of costs after taking account of exemptions and remissions via fees and charges



Source: National Audit Office analysis of HM Courts Service Accounts

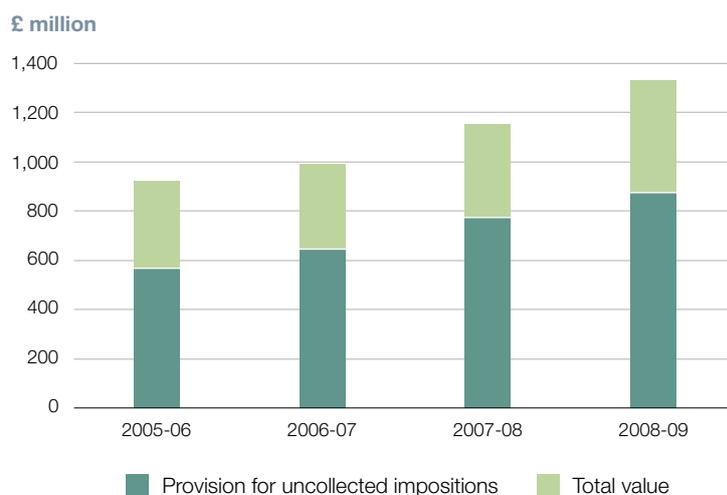
The value of outstanding impositions has increased

2.17 HM Courts Service is responsible for the collection of financial penalties imposed by the Crown and Magistrates' Courts ('impositions') including fines, costs and compensation. In addition, HM Courts Service is part of the Asset Recovery community and contributes to the collection of confiscation orders.⁹ Where fines and confiscation orders are in arrears and over six months old, the Ministry makes a provision in its accounts for them. The gross amount of outstanding impositions has increased from £920 million in 2005-06 to £1,330 million in 2008-09. Over the same period the provision for fines and confiscation orders in arrears has increased from £569 million to £875 million (**Figure 10**). Thus, only 34 per cent of the outstanding impositions balance is considered fully recoverable. Since 2003, there has been an increased use of Deduction from Benefit Orders for offenders who are in receipt of welfare or other benefits. This ensures payment is received but does take time to be paid in full, thus increasing the amount of impositions in arrears over six months.

2.18 In July 2008, HM Courts Service launched '*Criminal Compliance and Enforcement Services: A Blueprint for 2008 to 2012*' which focuses on 'first time' compliance with court orders, including financial penalties. HM Courts Service anticipates that this strategy will improve the collection of impositions and reduce the need for enforcement activities. HM Courts Service has been monitoring the implementation of the blueprint in each of its regions, but has yet to assess its impact. HM Courts Service plans to carry out this assessment in 2010-11.

Figure 10

The amount of outstanding impositions and provision for fines and confiscation orders in arrears over six months is increasing



Source: National Audit Office analysis of Ministry of Justice Resource Accounts

⁹ The Ministry is only allowed to retain a proportion of fines and confiscation order receipts under incentive and enforcement schemes. When collected, the remainder of impositions are not recognised as income of the Ministry, with fines surrendered to the Government via the Consolidated Fund and other impositions remitted to other Government Departments or victims of crime.

The Ministry's payment of creditors is in line with government targets

2.19 The Government has a responsibility to pay its suppliers promptly. HM Treasury reduced the 2009-10 target for payment of all trade suppliers from 30 days to 10 days¹⁰.

2.20 **Figure 11** shows that the Ministry is paying its suppliers promptly, with nearly 90 per cent of invoices being paid within ten days, in line with performance across government¹¹.

Figure 11
Ministry's supplier payment performance

Payment measure	Ministry (excl NOMS agency) ¹	NOMS agency ²
Average monthly value of invoices	£380m	£274m
Average monthly number of invoices	19,600	38,244
Proportion of invoices paid within 10 days	89%	88%

NOTES

1 Based on data collected from November 2008 to September 2009.

2 Based on data collected from April 2009 to October 2009.

Source: National Audit Office analysis of Ministry of Justice data

10 HM Treasury's Managing Public Money – Annex 4.6.

11 Report by the Comptroller and Auditor General, *Government Cash Management* (HC 546 2008-09). A survey of 14 central government departments and 16 sponsor bodies by the Comptroller and Auditor General found an average of 90 per cent of invoices were paid within 10 days in March 2009.

Part Three

Financial management in the Ministry of Justice

Introduction

3.1 Effective financial management is key to enabling the Ministry to meet its responsibilities for protecting the public, while also delivering value for money for taxpayers. This part of the report examines the Ministry's financial management against five criteria:¹² Financial Governance and Leadership; Finance for Decision-Making; Financial Planning; Financial Monitoring and Forecasting; and Financial and Operational Reporting.

Financial Governance and Leadership

3.2 The quality of financial governance and leadership within an organisation is fundamental if financial management is to be taken seriously. Sound financial management depends on streamlined accountability structures, and well developed internal control and risk management procedures.

The Ministry has improved its leadership structures

3.3 In April 2008, the Accounting Officer aligned the Board structure with the Ministry's four Departmental Strategic Objectives (DSOs), with each DSO headed by a Board representative. This simplified the accountability structures, and enabled the Ministry to manage both its delivery of objectives and its financial management better. The Ministry has two other executive members of the Board, the Director General Finance¹³ and the Director General Transforming Justice.

3.4 The Ministry has two appropriately experienced non-executive directors on the Board who provide complementary skills and external challenge to the Board's decision-making processes. One of the non-executive directors is a professionally qualified finance director of a public corporation and the other has extensive experience in employee engagement.

¹² See Appendix 1 for the source of the assessment criteria.

¹³ In February 2010, the Ministry appointed the Finance Director of the National Offender Management Service as Interim Director General Finance and changed the Finance Director's reporting line. The Ministry's previous Finance Director reported to the Deputy Permanent Secretary rather than directly to the Permanent Secretary.

The Ministry is yet to commit to a clear action plan for delivering its financial management initiatives

3.5 In March 2009, the Ministry reviewed its governance structures underpinning the Board. This led to the introduction of changes to its sub-committees as set out in Part One of this report, including the establishment of the Value for Money Improvement Committee to develop and oversee the Ministry's financial plans and monitor their delivery. To assist in aligning its financial management processes, the Ministry has brought together its financial management improvement projects, but is yet to commit to a clear, comprehensive action plan for the delivery of these initiatives.

3.6 In his report on financial management in the Foreign and Commonwealth Office,¹⁴ the Comptroller and Auditor General found that the Foreign and Commonwealth Office was able to generate significant improvements in its financial management processes by centrally coordinating its financial improvement plan under a change programme called 'Five Star Finance', with clearly stated aims and milestones for achieving success. The Ministry should ensure that it similarly articulates a clear statement of aims for financial management and focuses on the delivery of projects within its remit by including milestones and details of the resources required.

The Ministry has complex accountability structures

3.7 The Ministry delivers its services through a range of arm's length bodies and accountability structures. The Ministry's accountability structures in its executive agencies are complex, as illustrated in Figures 1 and 2 of Part One of this report, particularly in the National Offender Management Service, where the regional structure and local accountabilities in prisons, probation boards and trusts has made it difficult for the Ministry to integrate its financial management processes. This has affected the Board's ability to monitor the Ministry's overall financial performance and emerging financial risks in its largest executive agency.

3.8 In May 2009, the Ministry introduced an additional Audit Committee and accountability structures in the Access to Justice Group. While we found that this structure provides assurance to the Director General Access to Justice and corporate exposure for some of the Ministry's smaller arm's length bodies, we have identified overlaps between the accountability structures of the Group and the others within the Ministry's family. This resulted in duplicated frameworks for bodies within the Group. The Ministry is addressing this duplication by integrating the Access to Justice finance team with its Corporate Finance function.

¹⁴ Report by the Comptroller and Auditor General, *Financial Management in the Foreign and Commonwealth Office* (HC 289 2008-09).

3.9 The Ministry's largest Non-Departmental Public Body is the Legal Services Commission. In 2008-09, the Legal Services Commission's accounts were qualified by the Comptroller and Auditor General due to the level of error identified in the legal aid payments made by the Commission to solicitors. Both this qualification,¹⁵ and a separate Comptroller and Auditor General's Report,¹⁶ identified significant internal control issues in the Commission, including material irregular payments to solicitors, inaccuracies in the data held to make payments for legal aid and a lack of rigour in the review of the payments made by the Commission's internal assurance team. Although the Ministry had financial and operational monitoring structures in place, these systems were not able to identify the problems in the control environment at the Commission in time for the Board to address them. The Ministry subsequently commissioned the Magee Review of legal aid delivery.¹⁷ Following the conclusion of this Review, the Justice Secretary announced on 3 March 2010, the Ministry's intention that the Legal Services Commission would be converted from a Non-Departmental Public Body to an executive agency.

The Ministry has an established internal control and risk management framework

3.10 The Permanent Secretary, as Accounting Officer, has responsibility for maintaining an effective system of internal control to safeguard public funds and the Ministry's assets. The Ministry has an established risk management process, including the Corporate Risk Register, and the Ministry's Strategy, Policy Framework and Handbook were approved by the Board in July 2008.

3.11 The Ministry is required to produce an annual Statement on Internal Control for its Resource Accounts. This is informed by signed assurance statements, based on HM Treasury's Risk Management Assessment Framework, from each of the Directors General, and the Chief Executives of the Ministry's agencies and NDPBs, providing assurance on the operation of the internal control systems in their area of responsibility and highlighting specific risks. This process has produced transparent Statements on Internal Control since it was established in 2007-08.

3.12 The Corporate Audit Committee supports the Board and the Accounting Officer, is chaired by a professionally qualified non-executive member of the Board and comprises independent members. The Chair of the Audit Committee issues an annual report on the work of the Committee to the Board and Accounting Officer which is publicly available on the Ministry's external website. This is in line with good practice and shows that the Ministry is willing to be transparent in disclosing the Audit Committee's assessment of its risk management and corporate governance performance.

¹⁵ Report of the Comptroller and Auditor General to the Houses of Parliament on the Community Legal Service Fund and Criminal Defence Service Accounts for the year ended 31 March 2009 (HC 731 2008-09).

¹⁶ Report by the Comptroller and Auditor General, *The Procurement of Criminal Legal Aid in England and Wales by the Legal Services Commission* (HC 29 2009-10).

¹⁷ The Magee Review of Legal Aid Delivery: <http://www.justice.gov.uk/publications/docs/legal-aid-delivery.pdf>.

3.13 HM Treasury's Audit Committee Handbook, published in March 2007, recommends that both the Accounting Officer and Finance Director routinely attend Audit Committee meetings. The Accounting Officer has not attended the Committee since it was established and has delegated responsibility to the Director General Finance. However, the Accounting Officer has recently agreed that he will attend future Audit Committee meetings. This will enhance the Committee's influence in the organisation and his exposure to key accountability documents such as the Ministry's Statement on Internal Control and Resource Accounts.

3.14 The Accounting Officer and Audit Committee are supported by the Ministry's Internal Audit function. The Head of Internal Audit presents an annual report to the Accounting Officer on work undertaken during the year and provides an overall opinion on the assurance that can be taken from the internal control framework. The Ministry has also recently established a governance unit within Corporate Finance with responsibility for monitoring the Ministry's progress on outstanding Public Accounts Committee (PAC) recommendations, which has improved the Ministry's performance in monitoring these recommendations. The Ministry has also demonstrated its commitment to transparency by reporting progress against its outstanding PAC recommendations in its external performance reports. However, we found that the Ministry needs to do more to improve its performance in efficiently and effectively implementing internal and external audit and PAC recommendations. We also found that the Ministry's Audit Committee does not play a significant role in challenging non-implementation of recommendations and reporting non-compliance to the Board.

Financial Planning

3.15 The Ministry manages very large sums of money, including major projects and programmes delivered centrally and grants paid to delivery partners. The Ministry must, therefore, plan its future expenditure accurately to deliver its efficiency programme, whilst maintaining some flexibility to respond to changing priorities.

The Ministry's planning processes are focused on the short term

3.16 The Ministry's funding is linked to its DSOs and PSAs and is agreed with HM Treasury for three-year periods. As part of the Spending Review in 2004, HM Treasury set the Ministry an annual efficiency target by 2007-08 of £290 million. The Ministry reported savings of £455 million against this target, driven in part by staff reductions and relocation of posts away from London and the South-East.¹⁸

¹⁸ Revised targets are taken from the Ministry of Justice Resource Accounts 2007-08; outturn figures are from 2004 Spending Review: final report on the Efficiency Programme, HM Treasury November 2008.

3.17 The Ministry is in the final year of its current three-year funding settlement. The Comprehensive Spending Review 2007 set the Ministry a value for money target to generate annual savings of £1,077 million per annum by March 2011 and to achieve a 5 per cent real reduction in its annual administration budget.¹⁹ This equates to a total spending reduction of around 3 per cent each year in real terms. To assist the Ministry's planning for the delivery of this target, it requires each Business Group to provide a Medium Term Finance Plan to Corporate Finance at least annually, based on returns from individual areas. However, this short term focus, which includes the allocation of one year rather than three year budgets, restricts the ability of Business Groups to take a longer-term approach to planning.

The Ministry's Performance and Efficiency Programme has helped the Ministry to deliver its programme of efficiency savings

3.18 In response to the current savings target, the Secretary of State and the Permanent Secretary launched a Performance and Efficiency Programme to oversee the delivery of efficiency initiatives in October 2008. The Performance and Efficiency Programme includes agreed efficiency targets for each of the Ministry's Business Groups and for central initiatives, such as procurement. This focus has helped the Ministry to live within its budget in recent years despite increasing cost pressures in courts, prisons and probation.

3.19 The Ministry has reported that its value for money savings against the target for 2008-09 amounted to £329 million.²⁰ In August 2009, the Ministry's Internal Audit team examined the evidence supporting the savings against criteria established by HM Treasury. Internal Audit found that underpinning documentary information was not available to support the value for money savings reported by the Ministry's business units and questioned whether the savings could be substantiated against HM Treasury's criteria.

3.20 The Prison Service, which became part of the Ministry in 2007, undertook major reforms to its procurement system between 2004 and 2008, introducing a new procurement model with enhanced central control.²¹ This has resulted in prisons receiving more consistent supplies of goods and services, often at much lower prices than before. The number of staff directly involved in procurement was reduced from 481 in 2003-04 to 199 in 2007-08. Recognising the benefits of this process, the Ministry expanded this model across its operations in April 2009 in a project called Procurement Success. This has become a part of the Performance and Efficiency Programme and is expected to contribute over £40 million of savings by 2010-11, out of a total procurement spend of some £1.8 billion.

¹⁹ *Value for Money Delivery Agreement*, Ministry of Justice, February 2008, as modified by the 2009 budget and disclosed in the Management Commentary of the Ministry's Resource Accounts 2008-09.

²⁰ *Ministry of Justice Autumn Performance Report 2009* (Cm 7732). The Comptroller and Auditor General has agreed to review the efficiency savings reported by each Department and the underlying measurement and monitoring systems at least once during Spending Review period. For the Ministry, this work is due to take place in 2010-11, so the figures currently disclosed by the Ministry and included in this report are therefore currently unaudited.

²¹ Report by the Comptroller and Auditor General, *The procurement of goods and services by HM Prison Service* (HC 943 2007-08).

3.21 The Ministry has been effective in identifying and delivering ‘quick wins’, for example, in the rationalisation of its estate. However, further efficiency savings will require more fundamental changes to the criminal justice system. The Sussex Criminal Justice Board, which brings together local criminal justice agencies including the courts, probation and prisons, developed a pilot programme in 2009 to examine ways of integrating the whole criminal justice system. In addition, following pilots between early 2007 and mid-2008 within HM Courts Service, the Ministry is making progress in introducing LEAN methodology to its offices and courts to increase efficiency and effectiveness.²² These programmes demonstrate the Ministry’s commitment to delivering further efficiencies, but delivering significant change to the justice system will be difficult due to the range of external stakeholders involved in the process.

Finance for Decision Making

3.22 To make best use of its resources the Ministry’s Board needs to be able to make decisions on the allocation of resources to different activities, on the basis of accurate assessments of value for money. They also need a thorough understanding of the financial implications of policies, programmes and activities to monitor progress in implementation and delivery accurately.

The Ministry has programmes in place to establish the costs of its activities but they are being delivered too slowly

3.23 Accurate costing data is crucial in enabling an organisation to deliver its outputs efficiently. In the private sector the output costs of goods and services are used to judge profitability and compare performance. Sustainable cost reduction increases profitability and maximises shareholder value. Some areas of government expenditure are well costed and understood but, in a number of Value for Money studies, the Comptroller and Auditor General has consistently been unable to obtain accurate costing data for departmental activities.

3.24 In 2007, Lord Carter’s review of prisons²³ found that there was a wide variety of costs within the Prison Service, and recommended that it should improve its understanding of costs of prison places and activities. The National Offender Management Service, which now has responsibility for prisons, has a much better grasp of the cost of goods and services in prisons than was previously the case due to its centralised procurement system. However, 51 per cent of its costs²⁴ relate to staff expenditure, which is not recorded in a manner which enables costing of individual activities.

²² LEAN is primarily designed to eliminate waste and involves capturing the knowledge and expertise at local level to identify improvements and simplifications to processes.

²³ Lord Carter’s Review of Prisons: *Securing the future: Proposals for the efficient and sustainable use of custody in England and Wales* (December 2007).

²⁴ Source: NOMS 2008-09 Annual Report and Accounts.

3.25 Lord Carter recommended that the Prison Service should develop an operational specification for each category of prison, and a zero-based costing model to allow a better understanding of the cost and value of places and activities within the prison system. This would enable cost and best practice comparisons across the prison estate, and the introduction of a framework of service level agreements, similar to the commercial contracts in place for the private sector prisons. In 2008, the Comptroller and Auditor General similarly found that the Probation Service lacked information on the full cost of delivering community orders and needed to ascertain these costs to enable value for money to be determined.²⁵ The National Offender Management Service has taken these recommendations forward by developing a Specification, Benchmarking and Costing programme, which commenced in May 2008. The programme aims to develop and implement new costing systems, and define specifications for the various activities delivered in prisons and probation services to enable comparisons of relative cost and performance across the National Offender Management Service. The programme is progressing, is due to deliver improvements in 2010 and is scheduled to be completed by March 2012. It will cover all prison and probation services funded by the National Offender Management Service and delivered to offenders, defendants, victims and courts.

3.26 Collecting the data for this costing programme is very resource-intensive, requiring detailed observations of the activities in question. Challenges include the wide variation in characteristics of probation areas, individual prisons and the offender population. Whilst the exercise is starting to provide useful information, more needs to be done to improve prison and probation staffs' understanding of the importance of the programme and to deliver it more quickly.

3.27 HM Courts Service has developed an activity-based costing model through an extensive survey of tasks undertaken by Magistrates' Courts staff, such as the activities carried out by legal advisers. Further work is planned during 2010 to create similar models for Crown Courts and for the enforcement of fines. This model provides improved management information and provides a better basis for the allocation of costs, funding and staffing.

3.28 These initiatives will help to assist the Ministry to understand its cost base in more detail, but they will not be concluded for another two years. There is, currently, little coordination or knowledge sharing between the programmes in HM Courts Service and the National Offender Management Service, or the Ministry's other delivery bodies.

²⁵ Report by the Comptroller and Auditor General, *National Probation Service: The supervision of community orders in England and Wales* (HC 203 2007-08).

The Ministry's Investment Committee has enhanced the rigour of its appraisal of capital projects

3.29 The Ministry has delegated authority from HM Treasury to invest up to £70 million on individual capital projects. In May 2008, the Ministry created an Investment Committee to provide a challenge function for investment proposals in excess of £40 million. The Investment Committee, which meets monthly, is chaired by the Director General Finance and reports to the Value for Money Improvement Committee.

3.30 The Investment Committee receives business cases in a standard format based on the criteria set out in HM Treasury's Green Book for Appraisal and Evaluation.²⁶ The Investment Committee is supported by a panel of 'Keyholders', experts in each of the criteria, who undertake an initial detailed scrutiny and challenge of business cases before they are presented to the Committee. There is recognition throughout the Ministry that the Investment Committee challenges business cases robustly and this has led to an improvement in the quality of the submissions it receives. In addition, the Committee has helped to encourage the consistent use of business cases and investment appraisal across the Ministry's Business Groups and arm's length bodies.

3.31 In Autumn 2009, the Ministry introduced a process for monitoring projects classified as 'mission critical', once approval has been given by the Investment Committee, based on an assessment of value and relative risk. Monthly reports for each project are submitted by the project team to the Ministry's Change Division, assessing progress against key milestones and tolerances for five criteria: cost; benefits; people; time; and quality/scope. Quarterly reports on progress of the mission critical portfolio are presented to the Transforming Justice Committee together with additional reports on specific projects where the overall status has been Red or Amber/Red for three consecutive months. Once they are fully embedded, these changes will strengthen the Ministry's processes and will provide a robust framework for monitoring key projects.

The Ministry's Finance Directorate has insufficient visibility of the costs of policy proposals

3.32 The Ministry has a template for policy submissions which requires the financial implications of the policy to be set out. These implications are cleared with the relevant Business Group finance team, who are responsible for ensuring that the proposal is affordable and for monitoring subsequent expenditure on the policy. The Ministry is seeking to improve the process for formulating and delivering costed policy initiatives through its Policy Committee and from economists in local policy areas.

3.33 In our review, we found evidence that senior managers recognise the importance of policy submissions being supported by funding from the relevant Business Group, or other Government Department, and that difficult decisions may need to be made in the forthcoming spending review period. However, we also found that the Ministry's Finance Directorate does not have sufficient visibility of the costs of policy initiatives, weakening central control of the costs of the Ministry's forward policy programme.

²⁶ http://www.hm-treasury.gov.uk/data_greenbook_index.htm.

Financial Monitoring and Forecasting

3.34 Good quality financial monitoring systems allow an organisation to verify that its resources are being spent as intended. By monitoring and reviewing the costs of its key activities, the Ministry's Board can gain assurance that financial performance to date and forecast financial outturn for the year are in line with plans and consistent with operational performance.

The Ministry's multiple management information systems affect its ability to monitor its financial position and risks

3.35 The creation of the Ministry from the Department for Constitutional Affairs and parts of the Home Office has left the Ministry with a legacy of multiple data systems. The Ministry's Headquarters shares a financial system (Aramis) with HM Courts Service, the Tribunals Service and other smaller bodies within the Ministry's family; the National Offender Management Service uses a separate system (Phoenix) and the Ministry's large NDPBs (the Legal Services Commission, the Criminal Injuries Compensation Authority and the Youth Justice Board) and some other smaller bodies within the Ministry's family also operate their own individual data systems.²⁷ This limits the visibility of financial information across the Ministry's arm's length bodies. The Ministry is working towards integrating all its financial data onto a single system by establishing a combined Shared Service Centre covering the Ministry, its agencies and NDPBs by March 2013. This consolidation will help the Ministry to monitor financial performance across its delivery bodies more effectively.

3.36 The Ministry's payroll services are provided by a contractor, except for in the National Offender Management Service where they are provided by the Home Office. The Ministry maintains a database containing human resources information. We have found weaknesses in the quality of the information held on this database, for example the accuracy of the recording of staff transfers from the Ministry to other government bodies. The Ministry has recently improved this information and is now able to monitor its staff numbers centrally, but we found that managers are still using their own processes to monitor the numbers of staff in post in their area of responsibility. As staff payroll costs make up some 40 per cent of the Ministry's expenditure,²⁸ it is important that both senior and local managers have access to up-to-date, accurate and consistent information on employees from the same data source. This will be particularly important in the coming Spending Review where reductions in staff costs will make a significant contribution to future efficiency savings.

²⁷ The Ministry also operates a wide variety of operational systems, including the new Prison-NOMIS case management system currently being rolled-out in the NOMS agency and Libra, CaseMan and FamilyMan case management systems used by HM Courts Service.

²⁸ Source: Analysis of the Ministry's 2008-09 Resource Accounts.

The Ministry has yet to fully integrate its financial and non-financial performance information

3.37 In his report on Financial Management in the Department for Communities and Local Government,²⁹ the Comptroller and Auditor General found that the Department had made significant improvements in its financial monitoring through the development of integrated financial and operational performance reporting. Currently, the Ministry's monthly financial reports for the Board do not cover operational performance.

3.38 The Ministry reports operational performance on a quarterly basis via its Balanced Scorecard, which details performance for each of its four DSOs using traffic light ratings. Issues highlighted in these reports are selected for discussion by the Board, focusing on those areas rated as Red or Amber/Red. Financial measures covered by the Balanced Scorecard include progress against the value for money saving targets and the delivery of the Performance and Efficiency Programme. The monthly financial reports to the Board cover resource and capital spending by Business Group, but there is currently no link between the financial reports and the Ministry's operational reporting via the Balanced Scorecard.

Financial and Operational Reporting

3.39 The Ministry needs to demonstrate to its stakeholders how effectively it is spending its resources and what it is achieving. Internally, it is important that reports support management to make timely and robust decisions on the allocation of resources.

The Ministry faces a challenge in meeting the external financial reporting deadlines of the Clear Line of Sight Project

3.40 The Ministry produces annual Resource Accounts, in which it accounts to Parliament for the use of its allocated resources. HM Treasury requires Resource Accounts to be laid in Parliament before the summer recess, which in 2009 was 21 July.

3.41 Despite the challenging process of consolidating its executive agencies into its Resource Accounts, the Ministry has met HM Treasury's timetable since 2007-08, with its 2008-09 Resource Accounts being laid on 21 July last year. However, it remains one of the later Whitehall departments to lay its Resource Accounts. HM Treasury has initiated a 'Clear Line of Sight' project which aims to extend the departmental accounting boundary to include the Ministry's Non-Departmental Public Bodies and for departmental accounts to be laid by mid-June from 2011-12. This will present a significant challenge for the Ministry and it needs to ensure that its project plan for accelerating its accounts production timetable and the integration of its NDPBs is delivered.

²⁹ Report by the Comptroller and Auditor General, *Financial Management in the Department for Communities and Local Government* (HC 293 2008-09).

The Ministry's internal financial reporting is focused on income and expenditure and does not cover its balance sheet and cash flow positions

3.42 The effectiveness of Board decision-making is dependent on up-to-date financial and non-financial performance information being provided on a timely basis. The Ministry's Board receives monthly financial reports prepared by Corporate Finance. These reports are based on data collected from each of the Business Groups, but are currently limited to expenditure and income only and do not provide the Board with information on the Ministry's balance sheet or cash flow position. This reduces the profile of the Ministry's routine month-end processes, affecting the robustness of in-year monitoring processes, particularly of the Ministry's commitments and forthcoming cash requirements.

3.43 In 2009-10, the Ministry's finance team has sought to enhance the regular financial processes and produce quarterly in-year Resource Accounts for internal use. The success of this exercise has been limited due to the complexities involved in the process, such as the multiple financial systems and lack of a standard chart of accounts across the constituent bodies.

3.44 Board members have previously raised concerns about the degree of reliance that could be placed on the figures included in the financial reports. The Ministry's financial systems cannot automatically produce data for month-end reports in a useable form, so Business Groups must manually produce the reports for Corporate Finance. The Ministry has recognised the need for improvements to these processes and in March 2009 initiated a Finance Reporting Improvements Programme. As part of this, the Ministry has improved the reporting functionality of its financial systems and the accuracy of the figures, although further development is needed before staff are able to provide the information required using data taken directly from the financial databases.

3.45 The Ministry has also introduced changes to the format of the financial reports, which now include an analysis of key types of income and expenditure. This has been well received by Board members, but there is a need for further improvements, in particular, a more detailed commentary explaining the figures and providing an analysis of the issues for Board consideration.

Appendix One

Methodology

1 The National Audit Office developed its own toolkit for reviewing financial management from published methodologies, and this was used when undertaking the review. The approach followed the principles set out in the Audit Commission Discussion Paper *World Class Financial Management* published in 2005, and broadly accepted by the Treasury and other commentators. The toolkit identified a series of key statements on financial management under the five main criteria of financial governance and leadership; finance for decision-making; financial planning; financial monitoring and forecasting; and financial and operational reporting.

2 In making our assessment, guided by the toolkit, we used the following methods:

- semi-structured interviews with officials of the Ministry;
- an analysis of high level indicators of the Ministry's management of financial performance; and
- an analysis of departmental reports, Board meeting papers and minutes, guidance and reviews by external bodies, and previous National Audit Office research.

3 More detail on these methods is provided below.

Semi-Structured Interviews

4 We conducted interviews between October and December 2009 with several members of senior management within the Ministry, its agencies and main Non-Departmental Public Bodies. Similar themes were addressed in all interviews, with individual questions tailored to the specific individual.

Analysis of the Treasury Data on the Ministry's budgets and outturn

5 We analysed data published by the Treasury regarding the Ministry's Estimates; its budgets and expenditure. These publications detail the extent of and reasons for in-year adjustments to the original Estimates; enabling National Audit Office analysis of over and under-spends against each of the annual expenditure limits, and of the timing of the laying of audited accounts.

An analysis of Departmental papers

6 We examined a selection of Ministerial papers, Board meeting papers and minutes, guidance and reviews by external bodies, and previous National Audit Office research relating to the Ministry to identify best practice, future plans, and strategies.



Design and Production by
NAO Communications
DP Ref: 009262-001

This report has been printed on Consort 155 and contains material sourced from responsibly managed and sustainable forests certified in accordance with FSC (Forest Stewardship Council).

The wood pulp is totally recyclable and acid-free. Our printers also have full ISO 14001 environmental accreditation which ensures that they have effective procedures in place to manage waste and practices that may affect the environment.

Published by TSO (The Stationery Office) and available from:

Online

www.tsoshop.co.uk

Mail, Telephone, Fax & Email

TSO

PO Box 29, Norwich, NR3 1GN

Telephone orders/General enquiries: 0870 600 5522

Order through the Parliamentary Hotline

Lo-Call 0845 7 023474

Fax orders: 0870 600 5533

Email: customer.services@tso.co.uk

Textphone: 0870 240 3701

The Parliamentary Bookshop

12 Bridge Street, Parliament Square,

London SW1A 2JX

Telephone orders/General enquiries 020 7219 3890

Fax orders: 020 7219 3866

Email: bookshop@parliament.uk

Internet: <http://www.bookshop.parliament.uk>

TSO@Blackwell and other Accredited Agents

Customers can also order publications from:

TSO Ireland

16 Arthur Street, Belfast BT1 4GD

028 9023 8451 Fax 028 9023 5401

£14.75

