



The Government moved to a new resource-based financial management system from April 2001, with the implementation of accruals based accounting and budgeting in central government. The new system brings together central government planning, budgeting, Estimates and reporting on to a full resource basis.

The environment facing the Boards of public sector organisations is increasingly challenging, not only through the move to resource based financial management, but also as a result of other elements of the Modernising Government agenda. There is greater scrutiny than ever before of how efficiently and effectively public services are being delivered. Boards are being held accountable more directly for their management of resources and what they achieve from the consumption of those resources. There is a greater need than ever for transparency and the demonstration of sound financial management and robust performance management.

With these challenges comes the opportunity and necessity to use best practice performance management techniques and, in particular, to maximise the benefits to be derived from the new resource management information now available.

The aim of this booklet is to provide guidance to departmental Boards on how they can more effectively manage the resources at their disposal to deliver the outputs as defined by their Service Delivery Agreement (SDA) and so achieve the outcomes set out in their Public Service Agreement (PSA). It is aimed in particular at finance functions, and suggests how financial management information might most effectively be presented and interpreted to assist departmental Boards in their management role.

The guide also explains how financial management information can best be used to manage organisational performance, and suggests questions that might be asked to ensure that the right management information is provided. While the scope of this guide primarily encompasses departmental Board decision making, the principles explained in the guide are equally applicable to all public sector senior management teams responsible for organisational level performance.

The booklet is structured as follows:

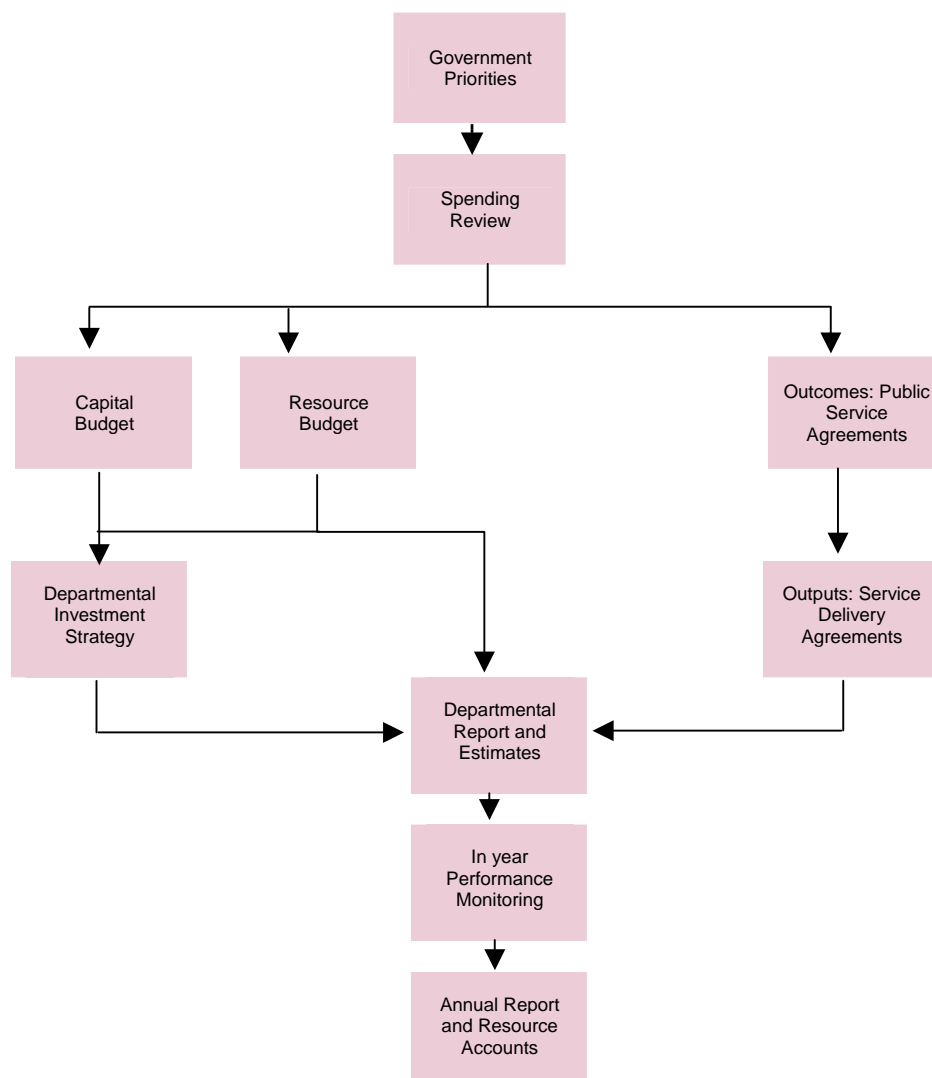
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# Board level decisions

Following the move to resource based financial management in central government, the Boards of public sector organisations now operate in a new public spending environment.

## New public spending environment



## Role of Boards

The needs of departmental Boards within this new environment will vary according to the scope of their responsibilities and the scale of the organisation's operations. However, there are common factors in the role of all Boards:

- **Strategic direction** – providing leadership and setting direction for the organisation.
- **Resource management** – identification and deployment of adequate resources to meet objectives, and managing people, finances and assets, including information assets.
- **Performance management** – accountability for performance, achieving outcomes, delivering against targets.
- **Corporate governance** – putting in place an adequate framework of internal control. Boards should ensure that significant business risks are identified, assessed, quantified, prioritised and managed, with independent assurance mechanisms also in place.



# Board level decisions

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## Board questions and decisions

- Given the different roles undertaken by Boards, there will be a need for management information related to their particular role. For example, at the time of the biennial Spending Reviews, Boards - acting in their strategic direction and resource allocation roles - are likely to need answers to the following questions:
- What outcomes should the department sign up to for the next three years?
- How will the department's PSA be delivered?
- What are the capital and revenue implications of the PSA/SDA?
- What are the cash flow and working capital implications of the PSA/SDA?
- What targets will be set for the organisation?
- What strategic programmes are needed to ensure success over the planning cycle?
- What risks are there to success and how will these be managed?

## Minimum requirement for Boards

- **A Board must not** be caught unawares failing to take action to:
- Meet the department's PSA and SDA
- Deploy resources to achieve departmental outcomes
- Avoid overspending its budget
- Avoid a Parliamentary Excess Vote – on resources or cash
- **As a minimum, a Board must** therefore have the necessary information (if only by way of exception reporting) on:
- Progress and estimated achievement against performance targets
- Progress on other strategic measures affecting the whole department and on which Ministerial or public attention is focused
- Expenditure to date and estimated outturn (DEL and AME)
- Estimated outturn on Parliamentary Request for Resources and on cash
- Supply and demand for people/skills to meet present and future needs
- Items on the departmental risk register which require attention

## Information needs

The departmental Board is therefore likely to require information on:

- Current performance against the existing PSA/SDA.
- Recommended SDA (that will deliver the PSA) - with alternatives, rationale and resource implications.
- Capital investment, cashflow and balance sheet implications of the PSA/SDA.
- Assumptions behind the figures.
- Sensitivity analysis around assumptions – what happens to intended outcomes if there is a variance from planned performance?
- The manpower/skill capability implications of the PSA and SDA.



# Board level decisions

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## Performance monitoring

The need for good quality management information for the Board in its performance management role is equally important. Questions that the Board should seek to answer include:

- What is the actual performance of the department's SDA against target and what impact does this have on achieving its PSA?
- If there is slippage, how significant is this and what are the options for recovery?
- Is there a need to reallocate resources? If so, what is the anticipated impact and what implications does it have for existing programmes/projects?
- How does actual capital and revenue expenditure compare to budget for Annually Managed Expenditure (AME) and Departmental Expenditure Limits (DEL)?
- What are the explanations for any significant variances from plan?
- Is the actual cash flow in line with budget, and what are the implications if it is not?
- How do the significant balance sheet balances compare to budget? What are the implications?
- Do the annual forecasts for each of the financial statements indicate difficulties later in the cycle?
- How are the financial figures linked to operational performance?

## Comprehensive management information

Delivery and interpretation of information required to support the Board's needs will be the responsibility of finance functions and other information providers. In particular, the typical current model is for finance functions to provide financial information and for non-financial information to be supplied from other sources.

If Boards are to receive all of the information they require to manage the department effectively, a comprehensive set of management information (financial and operational) should be supplied in a single coherent form. Boards should recognise that information may originate from different sources and establish the appropriate mechanisms to provide the necessary information.

## Delivery options

Delivery options will be determined by the particular requirements of the Board. Some good practice rules, which are attributes of good information that any reporting should aim for, are discussed in the following sections of this Guide:

- Providing decision-friendly information.
- Jointly presenting financial and non-financial information.
- Using exception based reporting.
- Providing summary level data.
- Performance management.

Each of the examples under these headings shown in the following sections is designed to indicate layout options only. The content is illustrative and is likely to vary in nature between organisations.



# Decision-friendly information

**G**ood quality information should help sound decision making. The information should provide interpretation to highlight significant issues and, where required, identify options and make recommendations. The information should be provided at summary level and should not therefore involve a large volume of reading.

## Example: variance analysis

The example below illustrates the use of financial information to show performance against original budget and forecast, and the projected full year impact. It also demonstrates how variances can be explained, implications highlighted, options explored and a recommendation made to assist boards in decision making. Colour coding is used to indicate variances within tolerance (black) and those that are more significant and require corrective action (red).

	Year to date					Full year			Notes
	Outturn £m	Original Budget £m	Variance £m	Revised Forecast £m	Variance £m	Budget £m	Revised Forecast £m	Variance £m	
<b>Costs</b>									
Staff Costs	18	15	-3	19	1	100	120	-20	1
Other Costs	11	10	-1	14	3	95	97	-2	2
Total Admin Costs	4	3	-1	4	0	10	11	-1	3
Programme Costs	10	8	-2	10	0	80	84	-4	4
Total Operating Costs	43	36	-7	47	4	285	312	-27	
<b>Balance Sheet</b>									
Working Capital									
Average Debtors	4	8	-4	6	-2	20	15	-5	5
Average Creditors	7	3	-4	8	1	20	25	-5	
Total	11	11	-8	14	-1				
Assets & Liabilities	25	24	-1						
Fixed Assets	67	68	1	67	0				
Cash flow	10	15	-5	13	-3	75	65	-10	
<b>Explanation for Variance</b>	1	Adverse staff cost variance is the result of ever increasing resource requirements in major projects which are now necessary in order to achieve the programme objectives.							
	2	Labour appears to be the limiting factor and increased labour costs are driving other costs elsewhere in the organisation. Additionally programme overruns are driving up programme costs.							
	3,4	See above (2).							
	5	Too many resources are tied up in working capital and hence a lower than expected a rate of return is being enjoyed on capital employed.							
<b>Implications (eg 5: Negative working capital)</b>									
Working capital is the difference between an organisation's current assets and its current liabilities. This includes the purchase of stock, the payment of salaries, wages and other business expenses. Its primary function is to support the day-to-day financial operations of an organisation. Liquidity problems could quickly arise if inflows and outflows of cash continually fail to coincide.									
<b>Options</b>									
(i) 'Do Nothing' and hope that actuals realign with budgets: this is potentially a very high risk option.									
(ii) Consider how the working capital cycle can possibly be reduced, thereby generating cash and profits more quickly.									
(iii) Examine relationship with creditors: eg have discounts for early payment been compared with the benefits from extended credit periods?									
(iv) Examine relationship with debtors: eg are effective credit control processes in place? Has debt factoring been considered?									
<b>Recommendations</b>									
(i) As a minimum, ensure the preparation of a cash budget to enable forecasts of cash surplus and deficit.									
(ii) Design and implement management reporting processes for occurrence(s) of significant variance.									
(iii) In the event of large surplus appropriate investments for cash should be considered.									
(iv) In the event of large deficits business should review expenditure, postponing non essential spending, or consider arranging a bank overdraft or loan.									



# Financial and non-financial information

**G**ood performance information should indicate both the implications of resource usage on the delivery of services, and the impact on the financial results of operational variances from plan.

## Joint presentation

Financial results and service delivery should not be reported separately, nor assessed in isolation. Accrual based management accounts should be reported throughout the year and presented jointly with the related operational performance.

## Example: financial and non-financial information

The example below shows the related financial and operational delivery status for three strategic programmes within an organisation. It combines financial, narrative and project milestone data in a single report.

Project 1			
	Budget £m	Actual £m	Variance £m
Week 1	25	25	0
Week 2	23	22	1
Week 3	24	27	-3
Week 4	20		
<b>Total</b>	<b>92</b>	<b>74</b>	<b>-2</b>

Project 2			
	Budget £m	Actual £m	Variance £m
Week 1	24	24	0
Week 2	23	23	0
Week 3	22	22	0
Week 4	19		
<b>Total</b>	<b>88</b>	<b>69</b>	<b>0</b>

Project 3			
	Budget £m	Actual £m	Variance £m
Week 1	23	20	3
Week 2	19	16	3
Week 3	18	12	6
Week 4	20		
<b>Total</b>	<b>80</b>	<b>48</b>	<b>12</b>

- Budget overspend in year to date (YTD) of x% due to extra spend last month to recover slippage in Programme 1.
- On budget YTD.
- Significantly underspent YTD reflecting slippage in activity (see below). Anticipate full year spend will be on target when activity recovers later in year.
- Programme 1 activity back on plan as a result of additional recovery spend last month (see above).
- Programme 2 on target YTD and anticipate delivery 1 month ahead of target.
- Programme 3 significant slippage due to planning application delays. Anticipate that slippage can be recovered later in year.



# Exception based reporting

As the objective of performance monitoring and reporting is to provide an indication of where corrective action is required, and to ensure that the attention of the board is focused in areas where it is most needed, exception based reporting should be used as a matter of course.

## Colour coding

Exception based reporting should take the form of reporting performance only in the areas where attention is required or highlighting areas of concern. The use of colour coding can be helpful in highlighting areas that are on target (green) or are deviating from plan and need attention (red).

## Example: exception based reporting

The example below illustrates a strategic project that is at “amber” (ie at risk of going significantly off target) overall. The major project components are shown at either “green” or “red” status.

## Workstream Status - Solutions

Current Successes	Current Issues
<ul style="list-style-type: none"><li>• Steady progress on test scripts</li><li>• Specs (now 40% complete)</li><li>• BPM site visits continuing</li><li>• 2<sup>nd</sup> workshop held on testing</li><li>• Constructive meeting with BM</li><li>• Solutions team moved to 5<sup>th</sup> floor – solved accommodation problem</li></ul>	<ul style="list-style-type: none"><li>• Business Blueprint delayed</li><li>• Software bugs encountered in latest version</li><li>• PTP will not be ready for CRP2</li><li>• Delayed start on process redesign</li><li>• Three weeks lost on establishing testing environment</li><li>• Need resource for inventory module</li></ul>

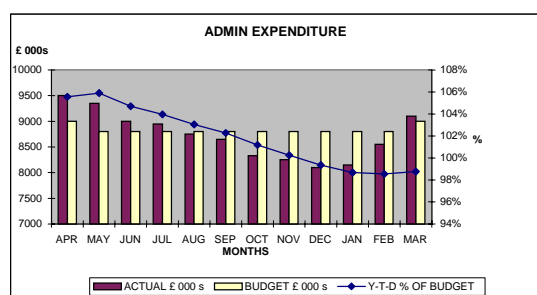


# Summary level information

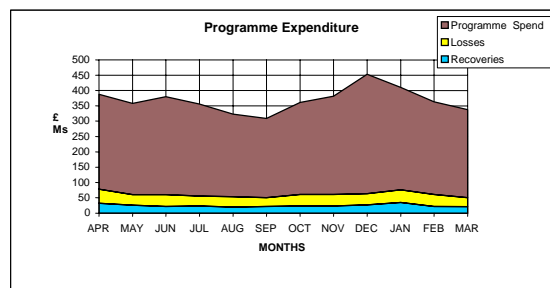
There is always a risk of information overload in providing performance reporting for a large and complex organisation. Information should therefore be provided at summary level to make the volume of information manageable and to avoid losing the key messages.

## Example: graphical presentation

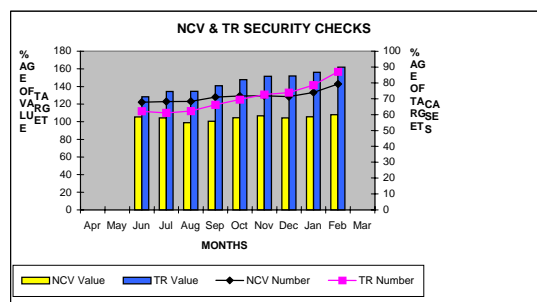
This approach can be aided by presenting information in graphical or pictorial form, which has the added benefit of conveying trend information more easily. In providing summary level information, it should always be possible to go to further levels of detail if required. A commentary is essential to put the figures in context.



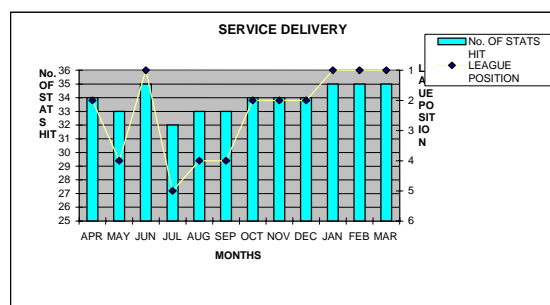
Annual expenditure outturned at 99% of budget reflecting marginally lower headcount than anticipated.



Programme spend followed the traditional seasonal pattern peaking in December and declining in the summer months. Losses continue to fall as % of total programme spend.



The security control programme continues to perform well with Targeted Reviews at 200% of target for value in the month. New claims visits were at 80% of target in the month for value due to staff shortages but are above target YTD.



Service Delivery performance continued at a high rate through the final quarter, with the region performing best in the country in each of the final three months.



# Performance management

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The “3 Es” – Economy, Efficiency and Effectiveness - are a good starting point in identifying what any board - irrespective of the purpose of an organisation or its size - should strive for, and what the related financial management information should seek to demonstrate.

## **Economy**

Economy means achieving results at low(est) cost. This can be delivered via appropriate tendering and procurement arrangements and constant pressure on costs.

## **Efficiency**

Efficiency is the delivery of greater output for the same resource consumption or achieving the same results at less cost. This can be demonstrated by showing historical trend information of how the organisation is faring year on year, or through external benchmark information showing how the organisation compares against industry norms or how particular functions or activities compare against similar organisations. Page 14 provides a link to further information on benchmarking.

## **Effectiveness**

Effectiveness means the organisation achieving its objectives. For government departments, are the SDAs being delivered and are these achieving the necessary PSA targets?

## **Performance management**

To achieve the 3Es, to direct and manage the organisation effectively and monitor performance, the board will require appropriate decision support information. Whatever the source of this information, the performance information system should reflect the FABRIC acronym. This means that such systems should be:

### **Focused**

- Is the performance information focused on the core aims and objectives of the organisation?
- What actions could the performance information provoke management to take?
- Why is the information being produced?

### **Appropriate**

- Do stakeholders receive the performance information they need?
- Is the right information presented in the right form for each group of users?

### **Balanced**

- Do measures cover all significant areas of work in the organisation?
- Are both financial and non-financial measures collected?
- Are indicators of future performance included as well as measures of historic results?

### **Robust**

- Can the system survive changes in personnel and in the structure of the organisation?
- Are there key people without whom the performance information system would not survive?

### **Integrated**

- Are the results of the performance information system monitored and used as part of the business planning and management processes?
- Is there consistent performance information at all levels of the organisation?
- Do people within the organisation own the system? Do they take note of the results and use them? Did they contribute to its design?



## Performance measures

### Cost effective

- Are the resources put into collecting performance information proportionate to the benefits derived for the organisation?
- What is the actual cost to the organisation of the performance information?

Good performance measures should be developed to meet the particular circumstances applicable in each case. The appropriate set of performance measures for a public sector organisation will be determined by the agreed targets set to reflect the desired PSA outcomes and SDA outputs. These can be presented in a performance management framework such as the Balanced Scorecard (discussed below). In any event, they should not be managed in isolation from strategy, planning and critical success factors.

Irrespective of the way in which the performance measures are developed, they should possess the following good practice attributes:

### Relevance

- Does the measure capture success in one of the organisation's key objectives?
- What does the measure tell you about how the organisation is performing?

### Encourages appropriate behaviour

- Does the measure encourage undesirable behaviour? For example, does it discourage people from admitting mistakes?
- Is it possible to improve performance against the measure without, in reality, improving performance?
- Does the measure allow innovation? For example, does the measure encourage challenges to the way a service is delivered?

### Attributable

- Can the measure be influenced by the organisation's actions?
- Is it clear where accountability for the measure lies?
- Is there an estimate of the degree to which the organisation affects the measure?
- Could a SMART (Specific, Measurable, Achievable, Relevant and Timed) target be set against the measure?

### Well defined

- Can the measure be expressed clearly, so that it is easy to understand?
- Does the measure have an unambiguous definition, so that it can be collected consistently?

### Timely

- What is the lag between the event and information becoming available?
- Does the measure provide information in good time for action to be taken?
- Does the measure provide information frequently enough for appropriate action to be taken?

### Reliable

- Is the performance measure accurate enough for the intended purpose?
- Has the measure been checked by relevant specialists?
- Is the measure responsive to change? Will it show significant changes in performance? Will the measure change because of random "noise" rather than actual performance variations?



# Performance management

## Comparable

- Does the measure allow comparison with past performance?
- Does it allow comparison with other bodies delivering a similar service?

## Verifiable

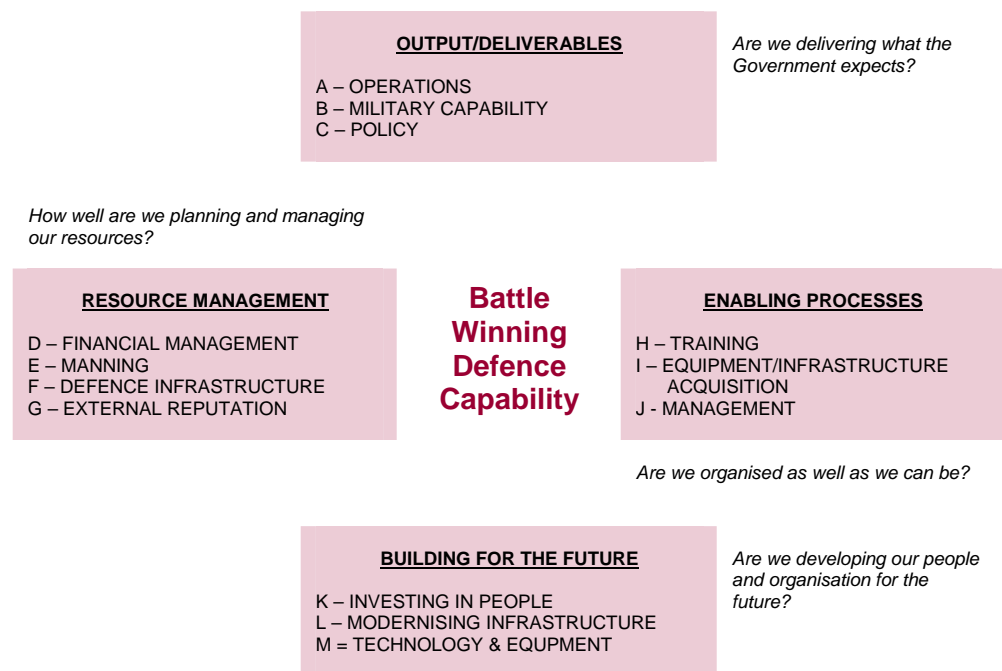
- Does documentation exist so that the process behind the measure can be validated?
- Is the documentation open to different interpretations?

## Balanced scorecard

The balanced scorecard is one way of ensuring that performance measures are developed as part of the strategic planning process.

A balanced scorecard is a format for describing activities of an organisation through measures for a number of perspectives. A good scorecard should describe the logic of the organisational strategy and help explain the cause and effect relationships that drive performance. A typical simplified scorecard, based on the Defence Balanced Scorecard 2002, is illustrated below:

### Defence Balanced Scorecard 2002



There is more to the scorecard than simply a collection of performance measures:

- The four perspectives aim for a complete description of what one needs to know about the business. First, there is a time dimension going from the bottom to the top: current delivery may largely be due to resource investment or process improvement in earlier periods. New skills added now should lead to improved service delivery in future years.
- The scorecard is also balanced in that it shows both the internal and external views of the organisation. Internal process, people capabilities and resource inputs are important, but only in order to deliver to the (external) customer. The scorecard reflects these different constituencies.



# Performance management

- The scorecard is linked through cause and effect relationships and assumptions, particularly when derived in connection with a strategy map. Among its most important uses is to reflect on how strong these linkages are, what time delays they involve and how certain they are under changing circumstances.

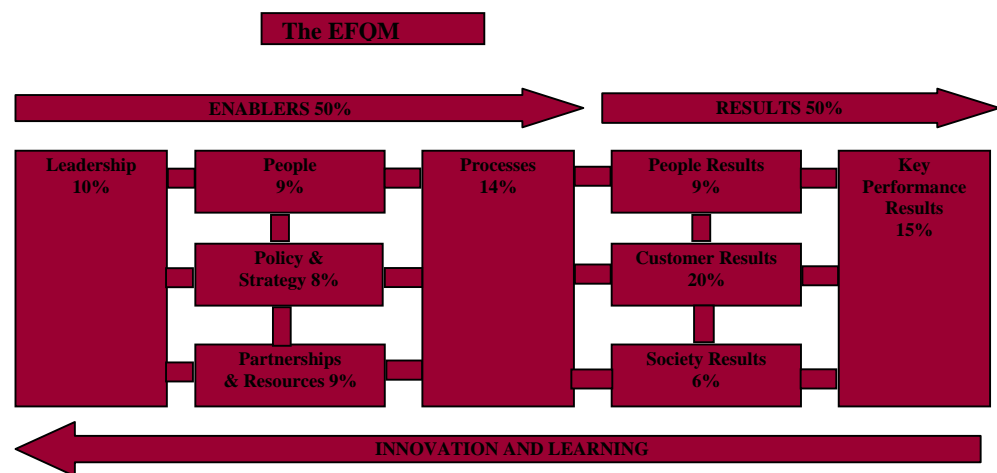
Links to further information on balanced scorecards and the strategy map are shown on page 14.

## Quality management

As part of the performance monitoring system, Boards should ensure that there are mechanisms in place to assure the quality of all key outputs. At organisational level, they should take steps to embed continuous improvement as a quality issue. At individual programme/project level, Boards should ensure that project management mechanisms include quality plans and that quality acceptance criteria are specified early in a project life cycle.

Also at the organisational level, boards should adopt a formal assessment and reporting mechanism such as the Business Excellence Model to encourage and monitor continuous improvement and so embed a strategic quality element in regular reporting.

The European Foundation for Quality Management (EFQM) business excellence model measures nine dimensions of organisational performance. These are grouped into “enablers” and “results” and are weighted in order of importance to overall organisational performance.



Links to further information on the Business Excellence Model are shown on page 14.



## Further information

### “Managing Resources” booklets

Further information on resource management issues is on the Treasury's website [www.hm-treasury.gov.uk](http://www.hm-treasury.gov.uk) and is included in many published documents. Booklets in the “Managing Resources” series (copies available from Anne Perryman e-mail: [anne.perryman@hm-treasury.gov.uk](mailto:anne.perryman@hm-treasury.gov.uk)) include:



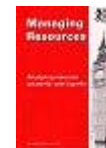
Full Implementation of Resource Accounting and Budgeting (the “Blue Guide”) – April 2001



Analysing resource accounts: an introduction (the “Short Red Guide”) – June 2001



Case studies (the “Orange Guide”) – January 2002



Analysing resource accounts: user's guide (the “Big Red Guide”) – June 2001



Reporting to the Board (the “Burgundy Guide”) – July 2002



Better decision taking in departments (the “Green Guide”) 2<sup>nd</sup> edition – July 2002



A strategic approach to finance training (the “Pink Guide”) – September 2001



Maximising the benefits for departments (the “Purple Guide”) – June 2001



Summary (the “Blue Leaflet”) – January 2002



Accountability (the “Chocolate Guide”) – July 2002

### Other guidance

Information on benchmarking can be found at [www.benchmarking.gov.uk](http://www.benchmarking.gov.uk).

Information on performance management is available in “Performance Reports for Boards”, a free guide from the CIMA Technical Services available on their website at [www.cimaglobal.com](http://www.cimaglobal.com) - look in their “Knowledge Bank”.

For further details on the balanced scorecard: “Translating Strategy Into Action: The Balanced Scorecard” - Robert S. Kaplan, David P. Norton, Harvard Business School Press, ISBN 0 – 87584 – 651 – 3; “The Strategy Focused Organisation” - Robert S. Kaplan, David P. Norton, ISBN 1 – 57851 – 250 – 6; and “Performance Drivers” - Nils-Goran Olve, Jan Roy and Magnus Wetter, Wiley, ISBN 0 – 471 – 49542 – 5

On quality and the Business Excellence Model: British Quality Foundation, 32-34 Great Peter Street, London SW1P 2QX [www.quality-foundation.co.uk](http://www.quality-foundation.co.uk), e-mail: [mail@quality-foundation.co.uk](mailto:mail@quality-foundation.co.uk). On risk: “Management of Risk: Guidance for Practitioners”, Office of Government Commerce, ISBN 0 11 330909 0.

