SUMMARY

Most local authorities manage their financial affairs well - in the sense of spending within budget and minimising irregularity - and have traditionally done so.

Councils' financial systems have maintained these strengths over many years, but they now have to cope with more rapid change than before - a new financial regime under the community charge, budgets delegated to schools and colleges and competition with the private sector. These changes set an exacting challenge to which councils must respond. And there will inevitably be tension between the need to maintain tight overall discipline (made more politically sensitive by the community charge regime) and the need for delegation in individual service areas.

Councils are also under political pressure to provide more responsive services than in the past to more demanding consumers. And traditional financial systems are not as good at encouraging effective management as they are at controlling the level of spending.

In The competitive council the Commission criticised local authority financial systems for placing unnecessary constraints on detailed management, and giving insufficient emphasis to overall performance. Its recommendation, expanded here, was to strengthen financial control by involving line managers more, and making them more accountable.

While local circumstances differ, in most councils four changes to the financial regime will help:

- ensuring that financial and management responsibilities are aligned, so that managers who make decisions are responsible for the financial consequences and more senior managers supervise their results;
- adapting ground rules, so that each manager has clear responsibilities and the incentive to manage efficiently;
- improving information, so that the right people are provided with clear, up-to-date information;
- improving advice, bringing it closer to line managers; streamlined central finance departments should monitor spending overall.

Councils taking these steps now report more motivated staff who manage budgets and services more actively all year round. This Management Paper expands on the four principles and suggests practical ways of implementing them.
INTRODUCTION

1 In its first Management Paper - The competitive council - the Commission discussed the emerging new consensus on local authority management, and set out eight key factors for success (Exhibit 1).

Exhibit 1
KEY SUCCESS FACTORS
The competitive council will...

1 Understand its customers
2 Respond to the electorate
3 Set and pursue consistent, achievable objectives
4 Assign clear management responsibilities
5 Train and motivate people
6 Communicate effectively
7 Monitor results
8 Adapt quickly to change

2 The paper stressed the important roles of councillors and the chief executive and of four management systems:

• **financial control**, to see that resources are used effectively and that budgets are not overspent;

• **policy planning**, a framework to decide the main issues facing the council and to match policies with resources;

• **performance review**, a system for monitoring the achievement of objectives and investigating how performance could be improved; and

• **people management**, to make sure that the right people are recruited, and that they are well trained and motivated.

3 Each of these important systems will be the subject of its own Management Paper, so the key issues of distributing resources according to a plan and of reviewing results and efficiency will be discussed elsewhere. But it is important that the systems work together, so the improvements in financial management advocated here would be strongly reinforced by other arrangements to set objectives, distribute resources and monitor results.

4 The competitive council outlined the Commission's main criticisms of many local authority financial systems:

— ‘they place unnecessary constraints on managers' ability to manage at the detailed level, while at the same time their performance may be subject to very little scrutiny;

— ‘managers perceive financial control as a constraint imposed from outside rather than as an integral part of their own job. Treasurers receive less cooperation than they should; their staff spend too much time on details rather than on strategic issues.’

The solution to these problems outlined in The competitive council is to strengthen central control of the total budget and the systems for setting objectives and monitoring performance. Line managers would receive better information and support, and have more explicit responsibility for budget totals and results achieved. Under this discipline, many detailed controls would become redundant.

5 This paper discusses these points in greater detail. It concentrates on the managerial arrangements for control of expenditure, rather than council members' role - also the subject of a further paper. The strengths and weaknesses of local authority financial management are considered first, together with some challenges to the traditional ways of working. Then new directions are explored. Inevitably, the strengths and weaknesses described are generalisations. Many councils are better, and a few worse, than the picture painted here.

TRADITIONAL STRENGTHS

6 Total council spending is almost always well controlled. Most authorities' expenditure is more or less in line with budget. In spite of some well publicised cases of budget deficits, underspending is still more common than overspending.

7 Standards of propriety are high. Frauds are rare and involve a minuscule proportion of council spending. The same does not apply in many other countries. Instances of major financial breakdown are well publicised perhaps because they are so unusual. Most British councils have strong balance sheets; nationally their assets are worth some five times their debt.

8 In short, overall spending is under control and almost invariably honest. These are significant achievements, especially given the complexity and size of the task. A typical county council, for example, spends £400 million on services as diverse as home helps and the police, provided from hundreds of service points. It is probably the largest landlord and employer in the area. Councils deal with hundreds of different suppliers and manage large capital programmes. They run trading operations, provide mortgages and issue bonds. They manage pension funds and provide financial support to local business.
9 How has local government maintained its strong financial base? Five factors are particularly important:

— a public service ethic, throughout the professions in local government, encourages responsibility and probity;

— a strong corps of accountants. This is a major difference from central government, which is significantly under-provided in this respect. The prison service, for example, with a £750 million budget has only two qualified accountants. A county council with similar expenditure would have 20 to 30;

— a clear budget focus. Council officers may not identify with or 'own' their department's budget, but they all know what it is. To many civil servants the budget is something announced by the Chancellor each spring;

— a wealth of comparable, detailed information, based on a standard way of keeping accounts. Local authorities know not only the unit cost of keeping a child in a council home, but can compare each of the elements of the cost of each different type of home. (The extent to which this data is constructively used varies considerably from place to place);

— a tradition of openness and scrutiny. Local government publishes this data,warts and all. (Although the practice is now at risk, with councils increasingly wary of publishing more information than their private sector competitors.) The peer group and political pressure to shine in comparison with others helps improve standards all round. Perhaps 150 years of district audit has made a contribution too.

10 Furthermore, local government maintained its financial strengths while real spending doubled in the 1960s and 1970s and through the reorganisation of 1974. New councils were created and old ones - often with different financial systems - merged. Financial discipline was maintained.

‘...overall spending is under control and almost invariably honest. These are significant achievements...’

THE IMPACT OF CHANGE

11 However, the pace of change has rarely been faster than today. Some is internally generated. CIPFA has introduced a new code of practice on accounts and is advising on control of capital costs and overheads. But most change results from central government initiatives. Four will make a big difference to the way a council’s finances are, or should be, controlled:

• the new financial regime: the whole landscape of local government finance will quickly become unrecognisable. The community charge, the national business rate, new capital controls and ring-fenced housing revenue accounts will alter the way in which councils think about their revenues and the cost of services. The Government’s objective in introducing the community charge is to increase local accountability. If the system works as intended it should increase the political sensitivity of marginal spending decisions;

• delegation to schools and colleges: under the education reform act most school governors and head teachers will be responsible for controlling their own budgets. Some councils previously introduced limited delegation, but now almost total delegation will be imposed on more than 13,000 schools. This will require major changes in accounting methods and the training of thousands of people new to financial management;

• competition for business: under the Local Government Act 1988, seven further services are required to compete with the private sector - refuse collection, street cleaning, grass cutting, catering (mainly school meals), building cleaning, vehicle maintenance and leisure management. Others could join the list soon. The Government has also tightened the existing compulsory competition rules on building and roads maintenance. Already competitive pressures are sharpening responsibility and clarifying the different roles of client and contractor. Demands for more control, better information, better advice and lower overheads come from those charged with competing - and infect the rest of the organisation;

• housing reforms: the local government and housing bill will probably mean increased pressure on rents. It will also give tenants the right to choose a new landlord. Councils wanting to keep their housing are likely to redouble efforts to keep in touch with tenants. This could encourage greater delegation to estate managers, or schemes where tenants themselves have some financial responsibility.
Each of these changes brings an opportunity. But each creates risk too - poor control in schools, badly costed tenders - unless management systems adapt to them.

12 Other changes may follow. A positive government response to the Griffiths report might make social workers responsible for community care budgets now controlled by the health service and private sector. The Social Services Inspectorate has recommended that all front line managers in social services departments should be trained to manage their own budgets, as some already are.

13 Increasing computerisation provides both an opportunity and a challenge to financial management. Delegation will encourage councils to link their schools up to the main computer. As well as allowing schools to keep their own records this will make major changes in financial administration economic at some time in the future. Information on payrolls, income, orders and payments to suppliers could be transferred electronically, with paper and clerical work reduced. Ultimately, this could reduce costs significantly, but not without substantial management effort in the mean time.

UNDERLYING PROBLEMS

14 Simply reviewing these changes together highlights one of the tensions councils will face in the coming years. Most of the changes which affect individual services argue strongly for increased delegation of financial responsibility. Yet this must occur within a new framework which is designed to impose an even greater need for tight overall discipline. Reconciling this tension will perhaps be the most difficult challenge facing local authority treasurers over the next five years.

15 In the Commission's view there is no necessary inconsistency between tight overall discipline and greater delegation. Indeed the latter ought - if it works properly - to enhance the former. But this is easy to say and difficult to deliver. The aim of this paper is to give some pointers to how it can be done.

'...most people in local government recognise that greater delegation of financial responsibility to line management makes sense...'

16 In principle, most people in local government recognise that greater delegation of financial responsibility to line management makes sense and some are acting to implement it. But greater delegation can only work well if objectives are clarified, efficiency and effectiveness reviewed. Financial structures also need to be adapted. The legislation is challenging many of the old methods of managing the council's finances. Some authorities have already grasped the nettle; others, while they recognise the need to realign financial responsibilities, still have a long way to go.

17 The first problem is that responsibility for financial control often fails to match management responsibility. In general, finance is still more centralised - either with the treasurer or at the centre of a service department. This has several counter-productive results. In particular it means that managers often do not 'own' their budgets and take too little responsibility for finance.

18 The mismatch leads directly to poor value for money and poor financial control:

— managers cannot respond to clients' needs. A general criticism is that the financial regime encourages low costs but not effectiveness. For example, the Commission's paper on services for people with a mental handicap argued for services tailored to each client's needs. But social workers can be sufficiently flexible only if they manage a budget which buys the range of services, from residential care to help with shopping. The audit of services for people with a mental handicap shows that this rarely if ever happens;

— they have little incentive for efficiency. Half the potential savings in the Commission's report on energy efficiency were from good housekeeping - switching lights off, closing doors etc. Opportunities like these are unlikely to be realised unless those directly involved can make use of savings for new projects;

— although financial control is good overall, it can fall down if too centralised. Information takes time to get to the centre and it is difficult for someone at a distance to put things right.

A specific example of the mismatch is that service departments using capital assets and receiving support services have had no financial responsibility for them, and so no incentive to use them effectively.
Secondly, many financial rules and procedures are restrictive, complicated and confusing. Many councils have relaxed virement rules over the last few years, but most are still unnecessarily restrictive and often more complicated than before. Savings on staff turnover might or might not be available for other uses according to intricate rules. There are sometimes lengthy negotiations about which savings or overspendings were the result of a manager’s actions and which outside his or her control.

A manager’s budget can be changed several times during the year when inflation or supplementary estimates are added to different lines in it. Recharges for central services can appear with little explanation of how they are calculated. Debt charges can vary with changes in financing policy. Costs are often charged to a manager’s budget without his or her knowledge or permission.

Complexities like these make the system difficult to manage and blur responsibilities. The rules exist for various reasons. Some are to improve control, and some to give incentives. But the combination can be confusing, lead to perverse incentives and have the opposite of the desired effect. Indeed, there are too many opportunities for gamesmanship with service department managers trying to get the better of the financial regime.

Thirdly, financial information is often poorly presented and out of date. Despite modern computer systems many line managers still rely on their own ‘black book’. Information often goes to the wrong people, badly presented and out of date. It comes in large, unwieldy computer printouts which are often poorly summarised, unclear, and off-putting. As a result, they often land up on a clerk’s desk rather than a manager’s.

Information on payments to creditors can be months late. An order effectively commits the money, but delivery can take a month and an invoice longer still. The payment might be made and appear in the council’s books in another month’s time, but it will have to wait for the next monthly run to appear in an expenditure printout. Commitments systems, designed to overcome this problem, are used with variable success. In the past, when relatively little financial control was delegated, all this may not have mattered much. Delegated managers were able to operate on a ‘black book’ system.

But there is now a clear need for enhanced information systems. Late and sketchy information gives little support to good managers, and dangerously little safeguard against management breakdown. The risk is most acute for difficult-to-control budgets like repairs, which could significantly overrun before anyone knew there was a problem.

The final weakness is related to the first. Financial expertise is sometimes too remote. The danger is that services do not benefit from good financial advice. Chief officers surveyed by CIPFA thought financial managers good at accounts, budgeting and audit, but much less so at advice. Ominously, given the advent of compulsory competition, commercial advice was particularly criticised (Exhibit 2).

Finance staff also form a small but significant overhead outside the control of the service manager. Service managers are looking harder at the value they obtain from that overhead, now that it may have a direct bearing on their ability to win contracts.
Weaknesses like these are not found everywhere. (Nor are the strengths of course.) And much is already being done to improve - most notably CIPFA's initiatives on support services and capital. But, in the Commission's view, there is scope for further improvement in most authorities, particularly given the requirements of the new legislation. With the different stages of development in different councils, it is impossible to prescribe a financial regime which would be appropriate in all cases. But as a general rule line managers should assume significantly greater responsibility for finance than hitherto. Implemented well, this shift of responsibility can enhance their jobs, increase their motivation, enable them to compete more effectively and provide more responsive services to their clients. Furthermore, it should strengthen overall financial control.

Enhanced responsibility for line managers must be combined with systems to set clear objectives and to monitor performance. The shift also requires four changes to the financial regime, correcting the weaknesses described above, if traditionally strong control is to be preserved:

1. Align financial and management responsibilities;
2. Adapt ground rules, to sharpen responsibilities and curtail gamesmanship;
3. Improve information;
4. Improve advice and streamline administration.

The following four sections discuss these steps and a fifth offers some advice on implementing them.

Some councils have already moved down this road, and where they have taken all four steps they have recorded a major success, with budgets actively managed all year round and line management strengthened. But the four changes do form a package. Greater delegation without, for example, information to back it up, is not likely to prove successful, and may be positively dangerous.

1. Alignment Financial AND MANAGEMENT RESPONSIBILITIES

Financial control will be ineffective and management poor unless those making decisions are responsible for the financial consequences. Otherwise, financial decisions may be made regardless of the effect on services and services may be managed without regard to finance.

Few would dissent from the principle that management and financial responsibilities should be aligned. Yet in practice such alignment is still not as widespread as it should be. This is perhaps not surprising, given the pace of change and the costs and risks of implementing new structures. But more needs to be done, and quickly.

An aligned structure of financial management needs to extend throughout the organisation, simply delegating responsibility to chief officers is insufficient. Four principles should lie at its heart:

- every budget should have a budget holder - and only one;
- front line managers should, as far as possible, be budget holders for items under their control, but for items that they cannot influence in practice;
- items excluded from front line managers' control should be managed elsewhere;
- senior managers should supervise the financial management of those reporting to them.

There are legitimate areas of discretion about the appropriate levels of responsibility. The principle is not to delegate as far down the hierarchy as possible. It is to make financial responsibility match the reality of management control. The box opposite suggests some ways in which this can be done, and the box on page 8 deals with capital costs and staff budgets - much the largest. The first step will almost always be a review of management structures and managers' real responsibilities.

The four principles above should make overall control of the budget more, not less, robust. The treasurer retains statutory responsibility for the council's finances. Indeed this statutory duty has recently been strengthened. But this responsibility is best exercised by making sure that the line management system works well, giving clear advice and using a robust set of 'early warning' mechanisms to monitor totals - rather than attempting to control too much directly.

The links in the chain of command between the treasurer and the individual budget holder are the key to aggregate control. As well as identifying the initial budget holder for each item, the budgetary roles of each tier in the management hierarchy should be clarified. (A clarification that could lead to a streamlined management structure.) Senior
HOW TO ORGANISE BUDGET HOLDERS

Before deciding the budget holder structure, think through case by case who should make which decision. There is no firm principle in favour of centralisation or delegation, but some general rules help.

Delegate responsibility when:

— a lot of short-term decisions are involved.

Larger, longer-term decisions are more likely to involve councillors or senior management;

— the service aims to respond to clients' needs. Leisure centre managers will be more effective if they can lay on activities to meet demand;

— costs are particularly dependent on individuals' actions and likely to respond to incentives. Energy or telephones budgets are good examples.

If budgets are delegated, organise a mix of:

— budgets like energy, that might respond to incentives but cannot be directly controlled; and

— equipment purchases that can be cash limited.

The ability to vary spending on equipment provides the incentive to keep energy costs down, and the safety valve for the budget total if energy costs overrun.

Don't delegate when:

— the need for expenditure is unpredictable and the costs might be significant enough to affect the delegated total. The obvious example is repairs. (Staff budgets are dealt with separately below);

— incentives would be perverse or undesirable. It might be wrong to allow individual managers to cut training costs if the council as a whole would suffer.

Arrange budgets so that the same manager bears the cost whichever alternative is chosen, e.g. in-house or outside provision.

EXAMPLE - housing department budget structure

Getting management and budget responsibilities right takes some thought. For example, the head of a children's home can manage much of the home's expenditure. But social workers decide how many children to admit. Their budget should recognise this.

Every item must have a budget, but discretion can sometimes be delegated without splitting and delegating the budget:

— a non-financial system (e.g. a staff budget) can be the means of control if discretion is only required over one resource (staff time);

but a delegated budget is needed where payments to outsiders are significant, or where one type of resource can be substituted for another.
HOW TO DEAL WITH BUDGET HOLDER DETAILS

OVERHEADS AND CAPITAL COSTS
Two important developments from CIPFA should improve the management of support services (worth some £2 billion a year nationally) and the use of capital assets (worth about £100 billion, excluding housing).

Traditionally, costs of capital finance and support services were only allocated to services as a paper exercise. Managers responsible for using them did not bear a real cost of doing so.

On support services, CIPFA recommends that:
- central departments (finance, legal etc.) should act more like contractors;
- they should reach ‘service level agreements’ with their clients;
- the cost of support services should be a real charge on clients’ budgets - if they use less support, they should have more money available for other things.

On capital, CIPFA recommends that:
- councils should compile a complete register of assets and a balance sheet representing their current cost;
- each service should be charged the economic cost of the assets it uses;
- the capital charge should be a real charge on each service's budget;
- a central account should collect in the charges to services and pay out for capital finance.

By analogy, the council centrally settles the mortgage for each asset and the service pays the council centrally a rent for using it.

Service departments should decide who is to exercise management responsibility for support service costs and buildings and organise budgetary responsibility to match. The head of a depot or neighbourhood office will very rarely have discretion to close their establishment, or to alter the payroll system for their staff. A senior manager in each department should therefore be appointed for support services, and another for premises. These people should be budget holders for the costs charged.

STAFF BUDGETS
Employee costs are much the largest item of council spending, and one of the most difficult to manage effectively, unless a cost centre covers a large number (50 or so). Neither complete delegation, nor centralisation is likely to work well:
- variations in staff vacancy rates would make a small delegated budget impossible to run;
- decisions about travel and overtime often need to be made by the immediate manager and cannot be controlled higher up.

In practice, management discretion is probably split between unit managers and their supervisors. Align budget responsibility with this practical split:
- delegate budgets for travel and most overtime to encourage efficient control of them;
- hold the main pay budget at a higher level, so that it covers enough staff to average out savings through turnover. This budget should cover the costs of temporary staff and overtime used to cover vacancies.

The budget holder and unit manager can negotiate case by case on how quickly staff should be replaced, and how to spend any savings made by agreeing an unusual delay.

REVIEW QUESTIONS

- Does every budget have one and only one budget holder?
- Are financial and management responsibilities aligned?
- Have management responsibilities themselves been clarified?
- Does each service department have a manager designated as client and budget holder for central support services?
- Do senior managers actively supervise their subordinates' financial management? Does the budget regularly feature on departmental management team agenda?

36 Any move to disaggregate budgetary responsibility - and such a move is now statutorily required in education departments - must be carefully planned. Managers should not be given budgetary responsibility without appropriate training and induction - or without clear and prompt feedback on their performance. The speed of change in education makes this difficult. Authorities must do their best in difficult circumstances. By starting now, it may be possible to move at a pace more commensurate with the scale of the change in other departments.
2. ADAPT GROUND RULES

37 After deciding the structure of budget holders and supervisory managers, the authority must clarify what they are responsible for. Ground rules should meet three objectives. Firstly, they should ensure that managers have incentives to control budgets and improve efficiency; secondly, they should make the system as clear as possible to operate, and as free as possible from gamesmanship; thirdly, they should ensure that budgets follow firmly from councils' political priorities, but also ensure that budget holders are involved in drawing them up.

SHARPEN RESPONSIBILITIES, GIVE INCENTIVES

38 The overriding principle is simply stated: budget holders must be in charge of making sure that the budget - and no more than the budget - is well spent to further council policy. But this is clearly not enough. Managers must know what happens when they overspend and what incentives they have to make economies. They must know the boundaries of their discretion.

39 A system of financial rules alone cannot see that money is used to further council policy. That requires a clear statement of policies and objectives, a definition of each manager's priorities in implementing them, and systems for monitoring personal and organisational performance. As these systems are put in place, detailed budgetary control becomes less necessary and could become an excuse for poor performance. Rather the emphasis should shift to control of budget totals - and that control should be strengthened through the active involvement of supervisory managers.

40 In practice many budgets are not amenable to cash-limited control (no one would sensibly advocate cutting all the telephones off if the budget were exhausted - though it has been done), so control can only be exercised over total budgets by insisting on the responsibility to make compensating savings. This puts virement (transfer of funds from one budget head to another) in a new light. Most council regulations regard virement as something to be restricted. But it should sometimes be an obligation.

41 Responsibility should not end with the budget holder, but should apply in the same way to supervisory managers, who may have to intervene actively to transfer funds between their subordinates or to help ensure better control. However, supervisory managers have a difficult role to play, and their training should stress the balance between intervention, to achieve their own objectives, and delegation, to increase their subordinates' level of responsibility.

42 By implication financial control should be concerned with the budget total rather than the details within it. And rules governing virement between different departmental budgets should primarily be the responsibility of departmental management rather than the treasurer. So a unit manager wanting to make a change outside his or her discretion should refer the question up the management line, rather than to an accountant. The Commission's research shows that this does not usually happen now - even where virement rules have been relaxed the detailed rules often mean that small virements need approval from departmental finance officers and accountants (Exhibit 3).

43 The logic is that most centrally administered rules on virement become unnecessary and should be replaced by much broader rules operating within each department and dealing with points of some principle. There are, of course, exceptions to this rule, which are discussed in the box on page 10. For example virements into staff budgets could create long-term commitments and should be limited, requiring authorisation from a senior manager.

44 Other rules should be examined to see whether they help or hinder. In particular, staffing controls are often as
restrictive as financial ones, or more so. It is acknowledged that control or monitoring of overall staff numbers by department helps to back up the financial system, and rules on some staff grades may be necessary to ensure comparability between departments. But as explained in the box, many other staff controls are superfluous.

45 Opinions differ on the problem of year-end spending - the rush to use the budget up before it is taken away. Many education authorities allowed complete carry forward of school capital, before the education reform act suggested extending it, and carry-forward seems to be more widely allowed in other budgets as each year passes.

46 In principle, there is no reason why the end of March should have any special significance for spending programmes, (particularly as spending no longer determines government grant) or why balances should not be carried forward. Certainly, there should be some way of allowing committees to carry forward significant sums earmarked for specific purposes. But it may make sense to carry out a thorough base-budget review to eliminate over-provision, and institute a system of resource allocation based on objectives, before widespread carry forward is allowed. If it is allowed - and this is one of the main problems of delegation to schools - it should be closely monitored and senior management should intervene before the sums involved get out of hand.

47 Gamesmanship and complexity are scourges of large organisations. They feed off each other. And the Commission is not naive enough to believe that the disease can be eradicated by good housekeeping. But different organisations exhibit different degrees of infection. Complex financial systems make budgets difficult to understand and manage, so one objective of reform should be greater clarity. Several changes recommended elsewhere for other reasons will help simplify: clearer responsibilities, virement and personnel rules are simplifications in themselves.

HOW TO MAKE SIMPLIFIED RULES WORK

VIREMENT RULES TO BE RETAINED
Keep rules where:
— projects are financed by grants or contributions from outsiders, especially joint finance;
— a limited number of projects have a high political priority;
— significant new projects are involved.
It would be wrong to give managers an incentive to delay new plans and use 'savings' to finance overspending on existing projects.
A general rule should prevent large virements that enter into a long-term commitment without a matching long-term saving. Most of these involve staff, so restrict virement into staff budgets.

STAFF CONTROLS
Controls on staff should be streamlined too, in accordance with four important principles:
• monitor the total establishment for each department, as one of the essential 'early warning' mechanisms. But detailed control of staff numbers in each section of a department is unnecessary;
• senior managers, acting as staff budget holders, should administer rules for overtime, temporary staff, travel etc.;
• rules on minor terms and conditions (leave of absence, working hours, working conditions) are usually agreed centrally, but can often be administered locally, subject to audit;
• some grading control is essential to prevent damaging precedents, but it often causes annoyance, if delay frustrates development or means that staff leave. It can be streamlined and speeded up:
— professions concentrated in a single department can be excluded from grading control - provided there is good budgetary control and a clear career development scheme;
— fix some timescale for central consideration of remaining controls - e.g. two weeks. Applications from managers to have their staff regraded should be deemed approved if not considered in this time.

• Are managers obliged to cut costs elsewhere if one budget overspends?
• Do they have incentives to make savings? (i.e., can service committees or managers redeploy money saved to develop their service?)
• Are senior managers responsible for supervising their subordinates' budgets and financial management?
• In practice, do they exercise this responsibility?
• Have the number of virements needing central approval been minimised? (How many were there last year?)

STOP GAMES AND SIMPLIFY THE SYSTEM
At least two further simplifications can be achieved. Firstly, with inflation lower than the levels reached in the 1970s there is little reason for constructing non-staff budgets at one price base and allocating inflation throughout the year. Doing so undermines the clarity which should be possible in a simple budget. A cash budget would not require amendment during the year. Central government budgeting moved onto a cash basis in 1978. Many local authorities have moved in the same direction. The education and competition legislation will require budgeting at outturn prices and in the circumstances it should probably be extended to all non-staff items. Staff costs are exceptional. Not only would large pay increases have a dramatic effect on an individual budget, but many of them are backdated to an extent which would make control almost impossible without a specific contingency provision to cover them.

Secondly, greater use could be made of standard costing - the technique in which a standard charge is made to internal consumers for each item (or unit of service). The consumer is then responsible for the volume of service required. The producer becomes responsible for any variations between the standard cost and the actual, which are controlled through a variance account. Standard costs are much easier for the consumer to understand and have the advantage that they are known immediately, so that management accounts can be much more up-to-date.

Many DSO operations are prime cases for standard costing, and CIPFA’s guidance on support services encourages it, but these are not the only candidates. If social workers assume the role of care managers envisaged by the Griffiths report, their budgets would have to bear the cost of the service provided to each client. Standard costs would be appropriate for each home help hour, or place in a children’s home. The home help, or children's home, manager would be responsible for delivering each unit of service at the agreed unit cost, and the social worker responsible for the volume of service consumed.

‘...Gamesmanship and complexity are scourges of large organisations. They feed off each other...’

A limited number of councils have tried to impose financial discipline through often complex rules. Unfortunately rules cannot make up for a lack of managerial authority, so they rarely work and only encourage people to look for loopholes or tactics to get round them - creative accounting at the departmental level. Thus, some rules designed to prevent overspending provide perverse incentives and positively encourage people to waste money.

Gamesmanship like this will never be abolished, but a clear and simple definition of responsibilities can go some way to reducing it. The main opportunities for gamesmanship occur around contingencies and budgeting - when the centre and departments negotiate. If bids to a central contingency fund are often agreed, departmental managers will be encouraged to make more of them - even when there is little hope of success the delay could provide an excuse for inaction. Asked to find savings, managers sometimes come up with the most politically sensitive items as an (occasionally successful) tactic to protect the whole budget.

The best response is to reduce the need for negotiation between departments and the centre, by encouraging departments to be self-reliant. In practice, the degree of self-reliance varies enormously. For example, some councils authorise literally hundreds of supplementary estimates (excluding inflation). Others allow only a handful for the largest and most unpredictable items - like the storm a couple of years ago, or the teachers’ work to rule. These two extremes lead to dramatically different cultures.

Inevitably things crop up during a year which could not have been predicted before it started. A prudent department, encouraged to be self-reliant, would put some of its budget to one side as a provision for contingencies. Most financial regimes prevent this, even where few supplementary estimates are allowed. These rules make self-reliance difficult and encourage fictional budgeting, as many managers may keep a hidden contingency fund despite the prohibition on doing so. There is a strong argument for allowing departments to carry their own contingency fund for all except the largest items. But there is a great danger that departmental managers would be over-conservative if the introduction of departmental contingencies was not initially controlled, and thereafter contained within a firm budget framework. Treasurers need to ensure, if departmental contingencies are allowed, that depart-
The budget system is at the heart of the financial regime and has to fulfil two, apparently contradictory, requirements. Firstly, it must represent the council's political priorities, and to this extent responsibility must be centralised with members. But secondly, it must involve budget holders if they are to own their budgets and feel responsible for sticking to them.

Budget time also provides the greatest opportunities for gamesmanship. Bids frequently greatly exceed the money available, so those who arbitrate on the budget get involved in detailed decisions about schemes in individual departments. If savings are needed they may have to look at the department's budget line by line - despite little practical or detailed knowledge.

The best way of avoiding this situation is to develop a simple but robust method of allocating budget totals without going into detailed bids. Individual service committees, and service department managers, would then be responsible for the detailed budget - within the previously agreed total.

Allocating budget totals without relying on detailed bids has several other important advantages. For example:

- a system can be developed for focusing on key policy matters and their broad resource implications, rather than being over-concerned with detail;
- actual or indicative budget totals can be set down in advance, and form a framework for service managers' plans;
- the longer lead time increases members' ability to make changes that could not be implemented in a single financial year;

HOW TO MAKE SAVINGS WHEN BUDGETING

The main system to match policies to resources should look more than one year ahead. Through this policy planning framework members can switch resources according to their priorities.

Although monitored centrally, the responsibility for efficient services rests with departmental management, reporting to service committees. The financial framework should:

- require management to review services, make efficiency savings, redeploy resources according to members' priorities and report on results;
- give managers confidence that they know in advance what will happen to money saved, and give them incentives to be efficient;
- assign some savings to a central pool, to finance new requirements and priorities.

Much of the responsibility for redeploying resources should be contained within each committee and department. For example, a social services committee might know that it had to save money on residential care to finance some of its extra community care.

Flag in advance where savings are to be taken to the centre, e.g.:

- plan in advance for demographic changes like falling school rolls, or growing elderly, and make it clear how the total budget will rise or fall;
- where priority has reduced, or studies show room for major efficiency improvement, agree in the plan how much the budget should fall each year to implement the savings;
- plan for a small arbitrary reduction in each department's budget total - e.g. X per cent of the whole budget or Y per cent of departmental administration costs.

In each case, service committees and management know in advance how much they have to save and have time to implement changes. If they can make bigger efficiency improvements, they can use the extra to improve or develop their service.

Central efficiency studies should also be conducted, for example covering property, energy etc. If management responsibility for any area is centralised, savings generated should be taken centrally too. After efficiency improvements have been implemented, the reduced budget can be reassigned to departments.

| HAVE PERSONNEL AND FINANCIAL RULES BEEN SIMPLIFIED? |
| COULD NON-STAFF BUDGETS BE CONSTRUCTED AT OUTTURN PRICES? |
| ARE STANDARD COSTS USED TO SIMPLIFY MANAGEMENT ACCOUNTS AND CLARIFY RESPONSIBILITIES, PARTICULARLY IN DLOs? |
| DO DEPARTMENTS SOLVE THEIR OWN PROBLEMS (DO THEY CARRY THEIR OWN CONTINGENCY FUNDS AND UTILISE SAVINGS), OR RELY EXCLUSIVELY ON SUPPLEMENTARY ESTIMATES? (HOW MANY WERE APPROVED LAST YEAR?) |
| ARE FINANCIAL RULES CLEAR AND SIMPLE? DO THEY AVOID PERVERSE INCENTIVES? |
| DOES THE COUNCIL'S CULTURE ENCOURAGE SELF-RELIANCE AND DISCOURGE GAMESMANSHIP? |

IMPROVE THE BUDGET FRAMEWORK

The budget system is at the heart of the financial regime and has to fulfil two, apparently contradictory, requirements. Firstly, it must represent the council's political priorities, and to this extent responsibility must be centralised with members. But secondly, it must involve budget holders if they are to own their budgets and feel responsible for sticking to them.

Budget time also provides the greatest opportunities for gamesmanship. Bids frequently greatly exceed the money available, so those who arbitrate on the budget get involved in detailed decisions about schemes in individual departments. If savings are
— discussions on future plans and efficiency reviews of existing provision can continue all year round, with more freedom from the budget timetable;
— budget-making should become simpler, with less of a last minute rush.

59 The development of such a system is important, but not necessarily easy, and a separate Management Paper on policy planning will discuss the issues in detail. It is also an intensely political issue. The Commission believes that better systems for policy-making can help councillors to become more effective. A further Management Paper will follow on the member role. In the mean time, the Commission's basic views on both issues are summarised in The competitive council.

60 Within this planning framework, delegation for budget construction can be delegated to service committees, senior managers and individual budget holders. As far as possible, the total should be set in advance, top down, which will reduce opportunities for gamesmanship. Budget holders should work from the bottom up (taking account of last year's inflation and virements) and suggest additional changes to improve services, make savings or respond to changing circumstances. Individual service committees or departments may well extend the planning system to a more detailed level than that approved by the whole council; it is then their responsibility to reconcile the figures that they planned to provide with the bottom-up figures prepared by budget holders.

61 It is easy to describe this approach in a theoretical way. It is equally easy to respond with world weary cynicism and hold that fine words on planning butter no political parsnips, that budgets will always be the sum of a number of political 'horse-trades' and that to suggest otherwise is the height of naivety. Yet many members and officers - if not all - acknowledge the need for a more rigorous approach. And some have developed systems which improve on what went before. The Commission's aim is to encourage such developments.

62 The treasurer, and other specialist staff, have four very important roles in the budgeting process:
— reviewing policy options to help inform decision-making by the council collectively, individual committees and managers;
— setting and monitoring budget guidelines to see that budgets are consistent and neither over-optimistic nor overcautious;
— advising on technicalities, such as inflation, contingencies, staff turnover etc., and on the process of reconciling the bottom-up budget with the planning guidelines;
— improving computerised systems, so that non-specialists can operate them and so that work can be minimised. In particular, some but not all financial systems allow changes affecting future years to be made at the same time as change for the current year. In this way a draft budget is produced automatically. Budget holders would need only to make further changes that they wanted to instigate. This automation should increase efficiency and reduce errors as well as simplifying the managers' tasks.

63 Managers should know how savings they make now will affect their position in future years. For maximum incentives, the benefit of savings should accrue to the service concerned. But councils all need to accumulate some savings at the centre. A solution to this dilemma - designed to maximise incentive and accrue savings at the centre - is discussed in the box on page 12. It is important to build confidence in these incentives and for managers to see them as real. There seems to be widespread cynicism at present that any savings made will be taken by the council centrally and that making savings is not worth the effort. This perception is counter-productive, but like most perceptions it will be difficult to change. Patience and some over-compensation - allowing people to make occasional mistakes - are needed if they are to gain confidence.

• Does the central budget process concentrate on policies and priorities? Does it provide at least indicative totals for each committee or programme for future years?
• Have budget totals been reviewed and systematic over-estimating eliminated? (e.g. over staff turnover).
• Is responsibility for detail delegated to budget holders?
• Could budget preparation be simplified?
• Are the rules governing 'savings' simple, clear and clearly understood?
3. IMPROVE INFORMATION

A successful shift of financial responsibility to line management depends on good, well presented information going to the right people as soon as possible. Out of date information can mislead, cause people to make the wrong decisions, or let a bad situation get out of hand. Bad reports can make it difficult for budget holders to control their accounts and undermine the supervisory responsibility of senior managers. Heavy or long computer tabulations inevitably end up on a clerk's desk, where a concise report should be in front of the director and on the agenda for the management team.

The vast majority of councils have basically reliable accounting systems, despite computer packages which rarely live up to their promise. This majority can concentrate on the, admittedly difficult, tasks of improving what they have, adapting it to cope with competition and delegation and making it more relevant to users' needs. For the minority, the overriding priority must be to make the basic systems work.

REPORTS TO THE RIGHT PEOPLE

Each budget holder should receive a regular budget report. This includes not only front line managers, but also those responsible for technical functions and senior managers who manage staff budgets directly.

Supervisory managers should receive summary reports for all the budgets of people reporting to them, in addition to a report for budgets that they manage directly. Each supervisory manager should receive a report with subtotals showing the bottom lines for those reporting to them. Additional reports could show alternative analyses by type of cost or policy area. Similarly, the treasurer and chief executive should receive a report on the financial position of the council overall and on the bottom line for each department.

At each level in the council hierarchy relevant budget reports should form a regular item on the management team agenda.

WELL PRESENTED

The presentation of reports is important. They must be brief. They must separate those items for which a budget holder is responsible from others (with a sub-total). Much less detail is needed for recharges ‘below the line’ than for the budget holder's main responsibilities. They should include a variance column and highlight areas of concern (Exhibit 4). The same points apply to information on computer screens.

Unfortunately most general ledger packages will not produce reports like this without a lot of work and it would be wrong to pretend that the process of improving reports will be easy. Some councils have abandoned standard packages and use 'fourth generation languages' (which automate much of the programmer's tasks and can be used by non-specialists) to generate their information.

Some councils make good use of non-financial information to supplement financial reports. (Usually combined with financial data on a micro-computer.) This can improve financial control and help monitor performance:

— some non-financial factors give a more direct and understandable indication of financial problems than a comparison of expenditure with the budget. Examples are staff numbers and staff turnover, the proportion of empty houses, occupancy rates and vehicle miles per gallon;

— other non-financial factors should be combined with financial data for performance review - looking at unit costs.

All budget holders should be able to get good financial information, but for those faced with competition it is vital. It can also need different treatment (see box on pages 16 and 17).

UP-TO-DATE

Late information undermines managers' confidence in budget reports. It also makes budgets harder to manage and provides a ready-made excuse for overspending. At worst a few councils have had to rein back well into a financial year because of overspending in the previous year. Some changes recommended above for other reasons will help speed up information. For
Exhibit 4
EXAMPLES OF BEFORE AND AFTER BUDGET REPORTS

Old Report
Many reports contain too much detail...

Alternative Report
...but could he summarised on a single sheet
example, with fewer supplementary estimates and inflation allocations, budgets themselves would rarely be out of date.

75 Turnaround time can also be reduced by encouraging budget holders to take information from screens as well as printouts and by printing reports in each office rather than centrally. Both facilities can allow for extra detail when required which helps in itself and means that main reports can be concise. Local production can also be psychologically important: managers generating a report for themselves are less likely to regard it with suspicion. Entering data in departments has advantages too. As well as cutting out paperwork, the computer can prevent users from charging costs to budgets that they do not control, and stop other mis-codings. Other ways of speeding up information are discussed in the box opposite.

76 Treasurers should set themselves two targets for their final accounts: by the end of May they should know how much each committee has spent and how much each committee has spent should be completed in time for the accounts to go to committee and be published well before the statutory September deadline. Despite this deadline 32 councils had still not published their 1987-88 accounts nine months after the year ended.

77 Improved information is important for two reasons: budget holders taking on new responsibilities will need im-

## INFORMATION FOR DIFFERENT USERS

Finance specialists and budget holders should discuss and agree the most appropriate reports for each budget holder. Much depends on the budget holder’s tastes. Reports (and screen formats) should be tailored to them. But the best presentation will alter according to level in the hierarchy:

- at senior levels trends and predictions are important, so show budget and expenditure for the month, to date and a prediction for the year end. Show extra detail by exception;
- for smaller budgets trends are less reliable, so show expenditure and budget to date, and the amount remaining for the rest of the year. Make it clear how commitments are treated: are they included with expenditure? shown separately? deducted from amount remaining? or not included at all? Make sure that the budget profile uses commitment assumptions consistent with the treatment adopted for them.

Ideally, all monthly reports should take account of commitments, but at least every quarter as accurate an assessment of commitments as possible should be produced for each budget holder.

### EXAMPLE: Report for competitive service: civic bar

<table>
<thead>
<tr>
<th>BACHESTER CIVIC BAR</th>
<th>BUDGETARY CONTROL REPORT TO END OF AUGUST</th>
<th>Year to date</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Budget</td>
<td>Actual</td>
</tr>
<tr>
<td>SALES</td>
<td>£000</td>
<td>£000</td>
</tr>
<tr>
<td>Bar labour</td>
<td>33.5</td>
<td>32.5</td>
</tr>
<tr>
<td>Cleaning</td>
<td>14.2</td>
<td>13.3</td>
</tr>
<tr>
<td>Total</td>
<td>47.7</td>
<td>45.8</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>CONTRIBUTION</th>
<th>£000</th>
<th>£000</th>
<th>£000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bar labour</td>
<td>0.3</td>
<td>0.2</td>
<td>66.7</td>
</tr>
<tr>
<td>Cleaning</td>
<td>1.0</td>
<td>0.9</td>
<td>90.0</td>
</tr>
<tr>
<td>Total</td>
<td>1.3</td>
<td>1.1</td>
<td>84.6</td>
</tr>
</tbody>
</table>

## INFORMATION FOR MANAGERS OF COMPETITIVE SERVICES

Management information should reflect the nature of the new businesses. Special analyses should inform business policy decisions and help cost tenders. Monitor non-financial indicators regularly, e.g.:
- labour productivity;
- stock levels and shortages;
- sickness;
- overtime;
- mix of work.

On the financial side:
- monitor costs and contribution for each contract, or trade;
- monitor key unit costs, e.g. per vehicle mile, per labour hour, per gully emptied;
- produce overall budgetary control information, which separates the main sources of variance.

Distinguish between businesses with income that is more or less determined for some time in advance (e.g. refuse) and those where it can vary from week to week (civic catering, jobbing repairs). In the former category expenditure control information may be enough, but in the latter monitor turnover and separate short-term fixed and variable costs (see Example below).

For further details of standard costing systems etc. see Part VII of Managing for competition produced by the competition joint committee.

### SOURCES OF VARIANCE FROM BUDGET

<table>
<thead>
<tr>
<th>Favourable/(adverse)</th>
<th>£000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Turnover</td>
<td>10.4</td>
</tr>
<tr>
<td>Expenses</td>
<td>19.3</td>
</tr>
<tr>
<td>Total</td>
<td>(5.6)</td>
</tr>
</tbody>
</table>

For further details of standard costing systems etc. see Part VII of Managing for competition produced by the competition joint committee.
E INFORMATION

MAKING INFORMATION MORE UP-TO-DATE

More up-to-date information is important, but not easily produced. Three things to do are (a) improve creditor and commitment systems, (b) profile budgets better and (c) reduce turnaround times.

CREDITORS AND COMMITMENTS

Creditors systems (which pay suppliers of goods and services) are very important for many budget holders as purchases are the most variable element of their budget. They are also the most likely to be out of date.

There are two problems:

- **bills received but not paid.** Most councils base their accounts on cash transactions and only add in debtors and creditors at the end of the year. By contrast, most commercial organisations keep debtors and creditors accounts throughout the year and make entries in their main ledgers when an invoice is received. The commercial system would make management accounts a month more up-to-date, and help to produce final accounts more quickly;

- **commitments.** Money is committed when an order is placed, often well before invoices are received. Many, but not all, councils have a separate system to help managers monitor commitments. Two problems are:
  - failure to monitor commitments at all;
  - confusion over systems used by local management but not central accountants.

All managers should have access to a commitments system, and if it is operated locally central accountants should take special care to ensure that the rules for operating it are understood, that outstanding commitments are periodically checked for accuracy and that summary reports including commitments are produced, perhaps each quarter.

Similar problems can arise when goods are ordered from stores, unless stores systems automatically make accounting entries.

BUDGET PROFILES

Budget profiles, (showing planned spending over the year) make interpretation of the actual results easier and at an aggregated level can compensate for the lack of a commitments system. A simple profile (with some exceptions) is to use last year's pattern of spending.

Otherwise, make sure that the profile compensates for the speed in which information comes through from the different systems. Payroll is likely to be up-to-date each month, but as creditors systems are likely to be behind, the profile for creditors should be offset by a month - starting at month two, and running through to month thirteen.

TURNAROUND TIMES

Reduce delays through:

- access to information on screens (with training support and screen formats pre-set to managers' requirements);
- more information punched locally, cutting out delays through paper-flows;
- quicker physical distribution of printed reports - maybe local printing;
- more frequent runs to update the main accounts from batch feeder systems, like stores.

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All of this advice on better information needs to be considered in the light of serious problems with most commercially available computerised accounting packages, the large costs of investing in a network to link schools, depots and offices, and the major management effort needed to implement changes in major computer systems.

proved support; senior managers in departments and the treasurer at the centre will need a good early warning system to ensure that any breakdown of delegated arrangements is spotted and tackled quickly.

- Do all budget holders and supervisory managers receive regular budget reports?
- Have budget holders been consulted on the form of their financial reports? And offered advice?
- Are they designed to match responsibilities and highlight significant variances?
- Are they brief?
- Are they used in practice? Do they appear on management team agenda? Do budget holders keep 'black books'?
- Is information as up-to-date as practical?
- Is the financial outturn for each committee available in May or June? Is the statement of accounts published before the September deadline?
4. IMPROVE ADVICE, STREAMLINE ADMINISTRATION

78 Those who assume greater delegated responsibility will need good financial advice, whether they are head teachers, managers of services trying to compete or other budget holders. Competition and delegation are bound to increase the demand for advice. But delegation should free the centre of some detailed responsibilities. Treasurers should therefore seek to redirect their staff’s work.

79 Computer developments may also significantly reduce the administrative workload at the treasurer’s department, and perhaps more significantly at the centre of service departments. Orders for goods, records of income received, pay and personnel details and requests for payment to suppliers could all be punched in directly in each school, depot or leisure centre and be carried out automatically. However, this would require very significant investment, and opinions differ about whether it will be justified in the short term, or as a more distant option.

80 One of the immediate priorities is to improve communications. Accountants and service department officers frequently do not understand each other’s point of view. Accountants should spend more time in the departments they serve. The treasurer should emphasise their responsibility to help solve management problems. Secondments to service departments should be organised and, where relevant, accountants could join departmental management teams or task groups. The chief executive of one county adopting this approach recently commented on its success: ‘seconded accountants are meeting the needs of their customers, but still maintaining the very strong links necessary with the central finance functions’.

81 Larger councils should consider the arguments for and against some form of decentralisation, with the twin considerations of minimising administrative costs and making advice as effective as possible, while preserving the treasurer’s independent ability to advise the council collectively. There are several options, none of which will be appropriate in all circumstances:

— **strengthening departmental finance staff.** Without decentralising anyone in the treasurer’s department, service departments’ finance offices could be built up and the treasurer’s department slimmed down;

— **physical decentralisation.** To help better communications and emphasise the importance of being part of the service department’s team, accountants could be physically located in the service department while the treasurer retains responsibility for them;

— **organisational decentralisation.** The most radical move would be to place the majority of accountancy staff directly on the service department’s establishment.

82 Even if accountancy staff move into service departments, the treasurer should retain responsibility for their professional and career development. The treasurer would be involved in their appointment, and positively encourage accountants to see experience in a service department as essential for a successful career in finance. Indeed there are strong grounds for strengthening the links between the treasurer and existing finance staff in service departments - through a system of joint responsibility.

83 No system of decentralisation can remove the need for independent advice at the centre. Indeed, delegation of responsibility increases the importance of a limited number of robust ‘early warning’ indicators.

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- Do accountants have an explicit responsibility to visit service departments frequently?
- Are they members of the management team or project taskgroups?
- How do service department managers view accountants? (Ask them). And how do accountants view service department managers? (Ask them too).
- Has financial advice been strengthened to cope with competition and delegation?
- For larger councils, have the options for decentralisation been considered? Is there a strong finance section in each main department?
- Has the finance department developed ‘early warning systems’ to detect serious problems before they get out of hand?
5. IMPLEMENTING THE IMPROVEMENTS

84 Councils should aim to gain the benefits of these improvements fairly quickly - especially where competition and the education act are forcing the pace - but it is important to recognise the amount of work involved, to make realistic plans, and to prevent serious problems during transition.

85 Three things will help to make the change successful:
1. Phase it in
2. Plan ahead
3. Concentrate on people management.

PHASE THE IMPROVEMENTS IN

86 The change in management rules and responsibilities recommended above is too great to be accomplished in one go, and an attempt to do so could seriously undermine financial control for that year. Phasing could work in four ways:

- moving down the hierarchy in stages - delegating to the swimming-pools manager first, and to the head of each pool afterwards;
- dealing with the costs in stages - taking supplies first and then moving on to staff costs;
- taking one department at a time;
- improving information and advice first, budget structures and rules afterwards.

A mixture may be best, providing it is not an excuse for inaction. For example a council-wide attack on financial information and advice could be combined with a pilot exercise introducing budget holders and streamlining rules for one department.

PLAN AHEAD

87 The council’s approach to phasing-in should be included in a plan, based on an assessment of strengths and weaknesses and the urgency of each change. Changes with a long lead-time (notably those involving computer systems) should start first. The plan should also help provide leadership and mobilise support for the improvements. The people who will become budget holders should be given a chance to understand the responsibilities that they will take on and the departmental chief officers encouraged to think through the effects on their departments.

88 Treasurers will also have to plan for some of the technical factors, discussed in the box below, which might otherwise undermine control during the transition.

HOW TO DEAL WITH THE TECHNICALITIES OF CHANGE

Altering the way budgets are run could cause technical problems, unless they are anticipated. Councils should be careful to:

- prevent unplanned increases in spending.
  Many councils underspend as a matter of course. Restrictions on virement and carry over mean underspendings go into balances and keep down rates or charges in subsequent years. Relaxed rules could cause unplanned increases in spending, unless systematic over-budgeting is eliminated. Take particular care over vacancy assumptions, and over-optimistic plans for service development;
- avoid accidental restrictiveness. If new cost centres are established before virement rules are altered, the interim system could accidentally become more restrictive in two ways:
  - if the number of budgets increases, and if virement rules extend to them (e.g. if a staff budget is created for each swimming pool, where previously there was a single budget for all pool staff). Transfers of staff costs between pools will need approval for the first time;
  - if the management responsibilities and financial rules move further out of line. Taking the same example, the system will also become more restrictive if each pool manager assumes budget responsibility, but the virement rules continue to apply to pools’ staff overall, pools’ energy overall etc. But transfers between one pool’s energy budget and another’s will rarely be made. Managers will want to transfer between supplies and services and energy for the same pool, but this would require authorisation;

Councils in both these circumstances have found the number of virement requests rocketing. The lesson is to alter rules at the same time as the budget structure;
- improve the quality of data. Opportunity for coding error increases with the number of cost centres. And errors assume greater importance in a relatively small budget. Training should be given to those completing basic documents, so that the importance of accurate coding is understood. Automation - pre-coded documents or computerised checks - can help too;
- try to prevent over-conservative budgeting.
  A significant problem may arise as the number of budget holders increases unless handled carefully. Finance department staff have expertise in predicting staff turnover, inflation and contingencies. But departments producing their own budgets may over-provide for these items. Treasurers should give firm advice. A scheme for phasing in changes could leave budgets at greatest risk until last, when departmental expertise has been built up.
CONCENTRATE ON PEOPLE MANAGEMENT

89 The whole point of these changes is to improve managerial behaviour. Good management of people is the key to success. The different amounts of attention that councils pay to people management is striking. Those which listen to their employees, communicate with them, motivate them, train them and supervise them effectively will have more satisfied staff and better services.

90 The effects of inadequate people management are as apparent in finance as elsewhere - too often managers are not consulted about the financial reports sent to them, or not properly trained to interpret financial data or use computer systems.

91 The needs of four different groups of people should be considered:

— senior departmental managers, who have to become committed to the change so that they can lead their staff. They also need to learn how to control their own budgets and how to take on the key task of supervising their subordinates’ financial management;

— front line managers, who will take over the bulk of the new responsibilities;

— departmental finance officers. Where they exist, they will have a key role in advising budget holders and senior management, in constructing budgets and tracking performance. They also have the main responsibility to improve the accuracy of coding;

— central finance staff, whose role will shift from control to advice. They will have to spend more time with service managers and less keeping accounts. They also need to develop monitoring systems to pick up problems before they get out of hand.

As a first step, efforts should be made to improve communications between the four groups.

92 One council that did concentrate on people when introducing new financial systems had more than 500 managers attend an open day in the finance department, where they met the accountants, saw displays, listened to talks, gained hands-on experience and took away brochures explaining the changes. Despite this effort, which was very successful in itself, the council subsequently concluded that it should have done more:

‘The mechanics of training, supporting, consulting and involving a large number of cost-centre managers were not fully understood then.’

* * *

93 Councils face many different, and conflicting, pressures on their management. And they come at a time when they find it hard to recruit and retain suitably qualified staff.

94 Some of these pressures - on budgets overall, for example - argue for a greater corporate approach. The Commission itself has stressed the advantages of corporate decisions on purchasing, for example, or cash flow management. Other pressures are centrifugal, pushing managerial and financial control out to service departments.

95 There is a difficult balance to be struck. The chief executive and the treasurer face the major responsibility, in consultation with their members. What is required in general terms is a new combination of loose and tight controls. In the case of purchasing, to take an example, the authority should ensure that individual managers are aware of the discounts available from central purchasing. If they have an incentive to save money, they will then use those arrangements.

96 The other challenge which senior managers face is to ensure that the management changes required are sensitive to the political process, or members’ ability to set objectives and see them delivered. Indeed the changes should make the organisation more rather than less sensitive to members’ wishes. But there is a danger that leading members (and chief officers themselves) perceive a loss of direct control, however illusory such control may have been in the past.

97 The way round this problem, and the path towards a redefinition of members’ roles and ways of working, will be sketched in a forthcoming paper.