Financial staffing and capacity within Local Government

Key findings

ACCOUNTS COMMISSION

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The Accounts Commission

The Accounts Commission is the public spending watchdog for local government. We hold councils in Scotland to account and help them improve. We operate impartially and independently of councils and of the Scottish Government, and we meet and report in public.

We expect councils to achieve the highest standards of governance and financial stewardship, and value for money in how they use their resources and provide their services.

Our work includes:

- securing and acting upon the external audit of Scotland's councils and various joint boards and committees
- assessing the performance of councils in relation to Best Value and community planning
- carrying out national performance audits to help councils improve their services
- requiring councils to publish information to help the public assess their performance.

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Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

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Introduction

1. We have identified a risk that staff in some support services may be under severe pressure after significant staff reductions. For example, information collected by auditors shows that most councils have reduced finance staff. Alongside this there have been an increasing number of references in auditors' reports to weaknesses in accounting systems.

2. As part of the 2014/15 audit auditors were asked to collect information on:
   - Organisational structure and the role of the Chief Financial Officer
   - Financial strategy and sustainability
   - Budget monitoring and reporting
   - Quality of the operational finance function
   - Finance staff capacity within the organisation
   - Financial Reporting.

3. This report pulls together common themes and issues on financial staffing and capacity in councils. The conclusions are drawn from the analysis of audit returns and commentary in the 2014/15 Annual Audit Reports for all 32 councils.

Summary

4. Chief Finance Officers (CFOs) continue to hold positions within councils that should allow them to deliver strong financial management. Twenty six of the 32 CFOs are members of Corporate Management Teams (CMT) or equivalent and as such are able to exercise influence at a strategic level.

5. All 32 councils produce an annual budget that includes revenue and expenditure. For the majority of councils this allows policy options to be assessed prior to the budget setting being finalised. Auditors confirmed that budget updates and supporting documents include sufficiently detailed commentary on each revenue and expenditure programme in order for decisions to be made.

6. There continues to be limited evidence of longer-term financial planning. All councils prepare short-term (1-2 year) plans and 29 councils prepare medium-term plans covering a period of up to five years. All councils need to develop long-term (5-10 years) financial plans which highlight the key risks and priorities and the long term affordability of service provision.

7. At March 2015, more than half of councils that had prepared indicative budgets for both 2016/17 and 2017/18 were reporting a funding gap between income and expenditure, even after they had identified savings and planned whether to use some of their reserves. The extent of the Scottish Government's funding reduction for 2016/17 is likely to result in councils identifying even larger funding gaps between the cost of delivering current services and the income they receive.

8. Priority based budgeting helps councils focus on the priorities it has set itself and then allocates resources to the services that will best contribute to achieving these outcomes. Twenty one councils have implemented a priority-based approach to budgeting.

9. Councils have reduced the number of staff in their finance functions with staff reductions at a service or departmental level. It is not clear if councils have appropriate succession planning in place to support future demands within finance departments.

10. To date the reduction in finance staff has had little or no overall negative impact on operational financial management with auditors reporting that the quality of unaudited accounts and working papers has not been affected. Some councils are planning to reduce finance staffing further. There is a risk that by further reducing finance staff, councils will not be able to carry out good long-term financial planning, effective monitoring of budgets and savings, and respond to the additional work involved in budgeting for the new health and social care arrangements.

11. An effective workforce strategy takes account of the skills needed for the future, not just the numbers and grades of staff. Councils will need to have the staff with the appropriate financial expertise to ensure councils focus on their priorities, aligning spending to the outcomes they want to achieve.

Key messages

Chief Financial Officers have an important role

12. In reviewing councils' organisational structure we aimed to determine whether the most senior finance officer is able to deliver strong financial management and offer strategic direction for the council.

13. CFOs have a range of titles from 'Head of Finance' to 'Executive Director of Finance' and the majority are members of the Corporate Management Team (CMT) (or equivalent). Thirty one CFOs, generally s95 officers, have a position within the organisation that should allow them to deliver strategic direction. The CFO usually reports directly to the Chief Executive and as a member of the CMT (26 are members of the CMT or equivalent) is able to exercise influence at a strategic level.

14. The CMT is responsible for overseeing the priorities and policies that have been decided by council members and implementing them in line with the council's strategies and financial plans.

15. The range and level of responsibility held by CFOs varies among councils. In addition to finance, CFO's may be responsible for a number of other departments including:
    - human resources
    - legal services
    - customer services
    - corporate services
    - information technology
    - procurement.

16. These additional responsibilities have been added to CFOs /S95 officer roles as a result of restructuring and service reform. Twenty-one of the 32 chief finance officers have additional responsibilities with 10 purely finance related. There is no evidence that these additional responsibilities affect the CFOs ability to ensure financial oversight at both a strategic and operational level.

Councils need to improve financial strategy and sustainability

17. In the context of overall reductions in public sector budgets, between 2010/11 and 2014/15, Scottish Government funding for councils decreased by 6.5% in real terms (allowing for inflation), to £10.76 billion. The 2016/17 draft budget has allocated total revenue of £9.4 billion to councils with further reductions in the Scottish budget likely.

18. We have previously reported the need for public sector organisations to undertake long term financial planning. **'Scotland's Public Finances: A follow-up audit'** report and our **An**

overview of local government in Scotland 2016 identified key features of financial planning that would enable CFOs to develop a longer-term approach including:

- Councils should have financial plans covering the short term (1-2 years), medium term (3-5 years) and longer term (5-10 years). These plans should set out the council's financial commitments, identify any challenges with the affordability of services and set out clearly how the council ensures its financial position is sustainable over an extended period.
- Long-term financial strategies covering a five to ten-year period to help: set the context for annual budgets; clarify the financial sustainability of an organisation over an extended period; and identify problems with affordability at an early stage.

19. Auditors reported that all councils have short term plans and 29 councils have medium term financial plans. Only 15 councils prepare long-term financial plans. These long term plans do not always contain the key features as outlined in **Scotland's public finances: A follow-up audit: Progress in meeting the challenges.** They are often high level strategy documents with little focus on expected changes to future income and expenditure and what actions may be required to meet objectives.

Case Study: Financial pressures facing councils

Argyll and Bute Council

The delivery of savings over the next 5 years will continue to remain challenging. The current budget gap is estimated to be between £21.7 million and £26.0 million over the period 2016/17 to 2020/21, requiring savings of between £7.9 million and £8.8 million in 2016/17 and between £7.9 million and £9.6 million in 2017/18.

East Dunbartonshire Council

The council is facing an increasingly challenging financial position. To address its projected budget savings of £23.3 million over the next three years, the council has been implementing a transformation programme. The Accounts Commission has highlighted that the council needs to have clearer priorities in its transformation programme to ensure critical projects are delivered and anticipated savings and benefits are realised. The council needs to improve important areas such as managing its workforce and finances.

Fife Council

The council faces budget cuts of up to £75 million by 2018/19. Transformational change will be required as recognised in the Executive Director, Finance and Corporate Services report to the Executive Committee on 18 August 2015 which stated that "…services cannot continue to be delivered in the same way as they currently are".

Source: Council Annual Audit Reports 2014/15

Budget monitoring should be linked to outcomes

20. Effective budgeting is important to ensure councils use the resources available to achieve the greatest benefit to the communities they serve. This will allow councils to set out where and how much resource needs to be allocated.

21. The development and scrutiny of setting annual budgets is an important activity, particularly during periods of financial constraint. All 32 councils produce an annual budget that includes all revenue and expenditure. For the majority of councils this allows the assessment of policy options where for others this has happened ahead of the budget setting. Auditors also confirmed that the budget updates and supporting documents include a satisfactory level of detailed commentary on each revenue and expenditure programme to help identify spending pressures and savings options.

22. Most auditors are satisfied that the financial information prepared for chief finance officers and members is at an appropriate level for management and strategic decision making. Reports highlight changes to budget and variances against budget, supported by satisfactory explanations. Seven councils do not directly reconcile current budgets to original forecasts, meaning the impact of budget changes is not clear.

23. The timeliness and frequency of reporting to members and senior management is similar across all councils. Senior management receive monthly budget monitoring reports and members as part of a relevant committee, usually receive quarterly reports. Although there is regular reporting, auditors reported examples of information being 3 to 4 months out of date.

24. Councils are facing increasingly difficult choices in how they reduce spending while providing existing services and maintaining service standards. The annual audit reports in 2014/15 comment on funding gaps and ongoing financial pressures being faced by councils. At March 2015, more than half of councils that had prepared indicative budgets for both 2016/17 and 2017/18 were reporting a funding gap between income and expenditure, even after they had identified savings and planned whether to use some of their reserves.

25. In August 2011, the Accounts Commission recommended that councils adopt a priority based approach to budget setting, which makes a connection between planned spending and intended outcomes and prioritises spending to achieve its objectives. This approach focuses on the priorities the council has set itself and then allocates resources to the services that will best contribute to achieving these outcomes. A priority-based approach helps councillors take decisions with a clearer understanding of the effect this will have on services.

26. By adopting priority based budgeting councils will be better placed to make connections between planned spending and the intended outcomes. Twenty one councils have implemented a priority-based approach to budgeting.

27. There is limited evidence that outcomes are linked to spending decisions. The need to consider outcomes is increasingly important as financial pressures continue and spending decisions impact on priorities and service delivery. Auditors reported that eighteen councils have a mechanism in place which allows them to monitor and report how the spending decisions that they are making are contributing to outcomes in the long term.

Case Study: Budget monitoring

Highland Council

We compared the council's five year revenue budget (2014 to 2019) against the important features of a financial strategy set out in exhibit 3 in Audit Scotland's national report 'Scotland's public finances: a follow up audit' and concluded that it could be improved. We also noted that budgets could be better linked to outcomes as some of its targets are unclear.

The council estimates that it will need to find savings of £46.3 million in the three years to 2018/19. To date, savings of £14.4 million have been identified. Difficult decisions involving the reduction and cessation of services and downsizing of the workforce will require to be made if the council is to deliver the remaining savings and balance its budgets over the next three years.

Source: Annual Audit Reports 2014/15

Quality of financial statements have improved

28. The reduction in financial staff has had little or no overall negative impact on operational financial management. In the main, auditors concluded that the quality of unaudited accounts and working papers has not been affected.

29. Auditors highlighted that there had been a noticeable improvement in both the quality of unaudited accounts and working papers or councils had maintained a high standard throughout the period reported. The auditor of Stirling Council concluded that:

- *the quality of the accounts and working papers has increased since 2011/12, and can actually be classed as examples of good practice. The accounts have been considerably streamlined to make them a far more useful document for all stakeholders and the timescale for preparation of the accounts and the audit process has been shortened considerably. This has involved very close working with the external audit team and the development of a good open and collaborative auditor/client relationship which has allowed these improvements to take place.*

There is ongoing pressure on finance staff capacity

30. There is an increasing risk that reductions in staff numbers will affect essential support services including the finance function within councils. 22 councils have reduced the size of their finance functions since 2011/12. '**Scotland's public sector workforce' published on 28 November 2013** reported that none of Scotland's councils had a workforce plan that covered the whole organisation. Instead they planned changes to their workforces at a service or departmental level. There is limited evidence that councils have appropriate succession planning in place.

31. The number of dedicated finance staff varies significantly across councils. The proportion of qualified finance staff to total finance staff also varies significantly. In the past, councils used

formal professional trainee schemes to help maintain the number of professionally qualified finance staff. Fifteen councils have a training scheme in place. Currently the number of professional trainees employed by all councils is 31, ranging from 1-7 in individual councils.

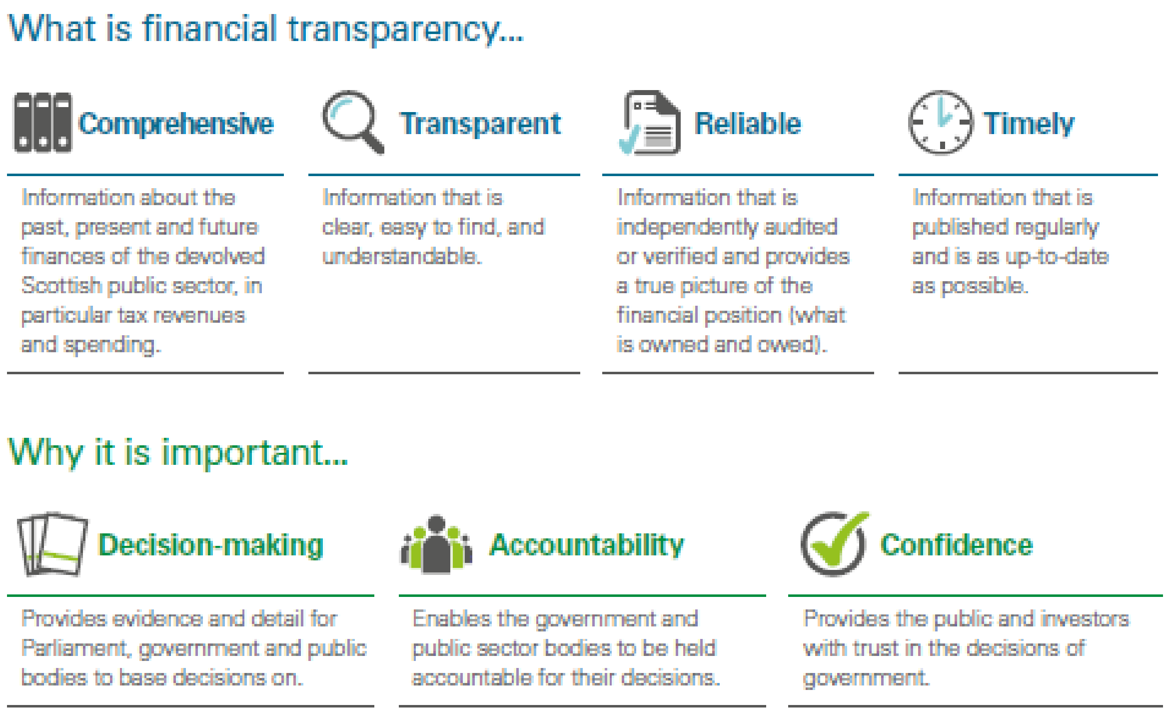
Looking forward

Councils need more transparent financial reporting

32. The case for comprehensive, transparent, reliable and timely financial reporting has always been recognised. It is crucial to show that public money is used properly and effectively. Clear reporting of local government finances is at the heart of financial transparency. It is important that the public are able to understand the public finances so that they can be involved in these choices. We have previously reported that better transparency and reporting is needed across local government and other areas of the public sector[1]. Exhibit 1 explains the elements that make up financial transparency and why it is important.

Exhibit 1

The importance of financial transparency



Source: Audit Scotland, Update on Developing Financial Reporting, March 2015

33. Transparency will help councillors and councils decide how best to use the money available to them, and allow them to be held to account for how the money is used. An overall picture of the financial position, what is owned (assets), what is owed (liabilities), and the composition of annual funding and spending, is essential to understand and manage the risks to financial sustainability. Financial transparency also supports effective scrutiny. Audit Scotland has produced guidance for councillors on scrutinising accounts.

34. Public reporting of financial information can take a number of forms, including audited annual accounts, budget documents and published plans. Budget documents, annual accounts and financial reports should be comprehensive, transparent, timely and reliable. This helps ensure

that councils have an accurate picture of their financial position; their financial prospects; the long-term costs and benefits of any policy decisions and changes; and the potential risks that they may encounter. It also provides councils and local taxpayers with the information they need to understand the financial position and to hold officers to account.

Long term financial planning needs to be better developed

35. The extent of the Scottish Government's funding reduction for 2016/17 is likely to result in councils identifying even larger funding gaps between the cost of delivering current services and their income, after taking account of planned savings or additional sources of income. Addressing this will require councils to go beyond incremental cost-saving measures to existing services and to fundamentally rethink their models of service delivery.

36. In setting budgets, councils need to focus more on their priorities, making clearer connections between planned spending and the delivery of outcomes. Rigorous use of options appraisal based on sound information is required for good budget-related decisions and making those decisions clear and understood. Exhibit 2 shows the options that should be considered when deciding on how to deliver services.

Exhibit 2

Source: An overview of Local Government in Scotland 2016, March 2016

37. There is mixed picture across councils when it comes to carrying out longer-term financial planning. Plans generally focus on the short to medium term up to five years. More work is needed to develop and regularly review long-term financial strategies that reflect priorities, risks and liabilities and the implications for affordability. Exhibit 3 illustrates what a longer term

financial strategy should include. Local government need to link planned spending more closely with the outcomes they want to achieve.

Exhibit 3

Source: Audit Scotland, Scotland's Public Finances, June 2014

38. Councillors have a crucial role to ensure they:

- satisfy themselves that their council has a longer-term financial strategy (five or more years) supported by an effective medium-term financial plan (three to five years). These should show how the council will prioritise spending to achieve its objectives, make any necessary savings and remain financially sustainable
- appraise all practical options for how to deliver the services their communities need within the resources available. This includes examining opportunities to work with and empower communities to deliver services in different ways, and learning lessons from others and from wider public service reform. They should ensure they get all necessary information and support from officers to help them fully assess the benefits and risks of each option.

Workforce plans must consider the skills required for finance staff

39. With their income falling further and as they identify funding gaps in the next two years or longer term, 24 councils are planning further staff reductions. Some councils are now making compulsory redundancies to reduce costs and better manage their workforces.

40. A number of councils have been developing their workforce strategies and plans. An effective workforce strategy takes account of the skills needed for the future, not just the numbers and grades of staff.

41. Information collected by auditors shows that most councils have reduced finance staff. Further reductions will increase risks for councils in being able to carry out good long-term financial planning, effective monitoring of budgets and savings, and responding to the additional work involved in budgeting for the new health and social care arrangements.

1 *An overview of local government in Scotland 2016*, Audit Scotland, March 2016, *Borrowing and treasury management in councils*, Audit Scotland, March 2015, *Major capital investments in councils: follow up*, Audit Scotland, January 2015