HB Publications

Strategic Financial Planning

for the public sector

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&
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Second Edition

essential skills for the public sector

Strategic

Financial Planning

for Public Sector Services

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ALTERNATIVE FINANCIAL STRATEGIES CONSIDERED

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Chapter 1

Introduction

In an environment where the demand for public services continues to grow, whilst often the financial resources cannot keep pace, managers need to become increasingly creative in the way resources are deployed by developing realistic financial strategies.

It may be considered that financial strategy should be left to the financial staff such as accountants, and finance managers. However, in organisations where operational managers often have "devolved" financial responsibility, they too need to be part of developing short and long term financial strategies.

This book considers how financial planning should be approached, such that appropriate financial strategies can be developed and implemented. Long range financial plans shape the future of the organisation and its ability to deliver the corporate, business and service plans. Financial planning should, therefore, be seen as an integral part of the overall planning processes. This text also looks at areas that are fundamental to supporting the financial planning process such as resource management, cost benefit analysis, and income generation. One option open to the public sector is to incorporate out-sourcing as part of a financial strategy to reduce costs. We consider the differences between public and private sector service provision, and the financial implications of both.

This book has been written as both a reference text and a development tool, which can be used by the reader as part of a self-development programme or to support recognised qualifications. At the end of each chapter are exercises and self-development activities, which can be undertaken by an individual or a team. The aim is to assist in interpreting the topics covered in each chapter as they are applied in practical and real life situations.

Strategic Financial Planning for Public Sector Services provides stimulating ideas for managers to think strategically about how they plan and use the finances under their control, in order to shape future service delivery.

This book is one of a series of “Essential Skills for the Public Sector” titles. The series aims to assist public sector managers become more efficient and effective in carrying out their important management responsibilities. We consider this book to be an important part of the tool kit for public sector management development.

Chapter 2

Financial Planning

Public sector organisations are responsible for the financial control of substantial amounts of public funds, and have a duty of care to ensure that those funds are well controlled and achieve value for money. In order to do this, a well thought out and robust financial plan against which to monitor performance is essential.

The Financial Planning Process

As with all plans, there needs to be clear aims, objectives, strategies, and action plans which are constantly monitored and reviewed. Planning should always be an ongoing process, and this is no different for financial planning. Ongoing financial monitoring should highlight whether or not the financial plans are being achieved.

The financial planning process is illustrated in the following table.

The Financial Planning Process
- a continuous cycle -

STEP 1:	Set objectives (may be for 1 or more years)
STEP 2:	Develop strategies to achieve the objectives
STEP 3:	Set out detailed action plans identifying targets, responsibility and timescales, along with detailed financial forecasts (budgets for income and expenditure, and cash flow forecasts if required)
STEP 4:	Implement action plan
STEP 5:	Monitor progress against planned targets and financial forecasts
STEP 6:	Modify actions to reflect the current position, set new targets, produce revised financial forecasts, etc.
STEP 7:	Review objectives to ensure they are still realistic and achievable
STEP 8:	If necessary go back to step 1 and set revised or new objectives

Financial planning cannot be undertaken in isolation and should be performed in conjunction with the organisation's other planning activities. Most public sector organisations will develop a variety of plans setting out the key aims and objectives for at least the year ahead, if not for a longer period. The objectives identified in these plans will only be achieved if the financial resources are available to support them. Financial plans are critical in determining whether or not the objectives are realistic and achievable.

Depending upon how the organisation is structured, there may be a range of plans produced for a variety of purposes. An illustration of the plans produced by public sector organisations, and the type of financial information that should be included, is shown as follows:

Type of Plan	Purpose	Financial Plan
Corporate Plan	Sets out the organisation's overall vision. It should identify the organisation's general aims and key objectives that need to be achieved, and may be used as a framework for the development of all other plans.	Should set out the planned income and expenditure for the whole organisation, clearly stating the sources of expected income and the key expenditure areas.
Departmental Business Plan	Within the context of the corporate plan, the department should specify departmental objectives, which should be SMART (Specific, Measurable, Achievable, Realistic and Time-related) in nature. It should identify how the department is organised and how the organisational structure will deliver the objectives. The action plans may be broadly based, but responsibility for achievement should be clearly defined along with timescales. This plan will provide the framework for all plans developed by the service units within the department.	The departmental budget should reconcile with figures produced in any of the other plans. How the budget is allocated between service areas, should be part of the departmental financial planning process. The budget allocation should allow service units to deliver the objectives identified in the plan. The financial plan should, therefore, provide details of the proposed income and expenditure for each operational or service unit, along with information on how the funding requirements for both revenue and capital expenditure will be achieved.

Type of Plan	Purpose	Financial Plan
Service (or Business) Plan	Most large organisations will organise their activities on the basis of service areas. These may be broken down into cost centres, business units, service units, etc. and it is now common for each service area to produce a service or business plan with respect to their activities. This plan should be more detailed than the plans previously mentioned such that they can be used as a working document. The content will include SMART objectives, strategies and action plans and should be used as part of the day-to-day management of the service. Service performance should be monitored on a regular basis against this type of plan.	The financial plan should be detailed with respect to month-by-month expected income and expenditure. It should ideally be "profiled"[1] based on the planned service activities. The overall net expenditure budget, should agree with the service's budgeted expenditure set out in the departmental plan. The financial plan should be used as a regular monitoring tool for the service, and be part of the financial management and control process. There should be a clear link between service objectives, service output and the financial input. This can be achieved by adding a unit cost dimension to the financial plan such that productivity can also be monitored.

[1] "Profiled"- reflecting the timing of income and expenditure over the period

Type of Plan	Purpose	Financial Plan
Operational Plans	In some organisations, there may be certain operations that cut across departments and/or service areas, and these operations also require plans. These tend to incorporate activities such as marketing, human resources, facilities management, communications, contract management and so on. These operations may become business units in their own right, or may be co-ordinated functions spread across the whole organisation. The operational plans should take on a similar format to the business plans described above.	The financial plan for operations may need co-operation and/or collaboration across a range of service areas or departments. The plan should be developed in the same manner described for the business or service plan. However, it is essential that the funding of operations is clearly identified, particularly where it is dependant on budgets arising from different sources.

In order to produce meaningful financial plans, there needs to be a mix of bottom-up and top-down communication as follows:

The corporate plan developed by senior managers, should be widely communicated such that all personnel understand the organisation’s core objectives, the wider financial picture, and the available financial resources.

⇩

Service managers should then identify the level of financial resource they require, in order to deliver the objectives set out in their business plans.

⇩

When the financial plans of all the service managers are consolidated, the total financial requirement should fit within the organisation’s overall financial resources.

⇩

Should the total requirement be greater than the available resources, this must be communicated downwards such that service managers can amend their business plans given the financial constraints.

Short term and Long term Financial Planning

Use of the phrases “short term” and “long term” planning vary considerably from organisation to organisation (the short term is often seen as 1 to 3 years, and the long term 4 to 10 years). In the public sector, however, the planning cycle tends to be short term, as long term planning can often prove to be very difficult. Two important reasons for this difficulty are the funding regime (funding is sometimes agreed annually, or for up to a 3 year period), and the political environment (involves regular central and local government elections every few years with each leading party having differing priorities).

Given the types of services being delivered by the public sector, strategic financial planning should ideally span a longer period of time (e.g. 10 years plus), incorporating both short and long term plans.

Some examples of long and short term financial objectives are shown as follows:

Exercise 3

Financial Decisions

You are the new Director of Finance taking up a position that had been vacant for the last 3 months. It is currently mid way through the financial year, and a number of resource issues have come to light where your input into the decision making is critical. The organisation's overriding objectives are to ensure budgets are not breached and service levels are maintained.

You have been presented with the following list of problems, along with a number of options in each case, and you are expected to give guidance as to the best decisions to take in the interest of the organisation's long term financial position.

Problem	Options
The capital programme is in trouble. One project with a value of £2.5m is delayed by 6 months, and 3 projects are due to exceed budget by 10% totalling £1m	(a) Begin a substitute project and use the £2.5m within the timescale. Seek to raise the £1m overspend from sale of assets (b) Use £1m to fund the overspends on the 3 projects, and identify another project to utilise £1.5m (c) Review the overspending budgets with a view to bringing expenditure back on track. If possible invest the £2.5m until the project can be started
Decision	

Problem	Options
The salary budget appears to be overspent by 10% due to the heavy dependence on temporary staff provided by agencies	(a) Renegotiate contract arrangements with agencies and force down rates, otherwise do not use the agency (b) Recruit and fill vacancies, allow services to decline in the short term to generate savings (c) Establish flexible working to cover absences and cease use of agency staff
Decision	

Problem	Options
Two properties have been put up for sale by auction and failed to meet their reserve prices (£300,000 each).They are both in a poor condition and require £250,000 investment in repairs. Doing nothing will result in the values declining and the cost of repair increasing	(a) Re-auction with a lower reserve price (b) Fund repairs by cutting an alternative capital project, undertake the repairs, and re-auction at a higher price (c) Seek partnership funding to undertake the repairs, and bring buildings temporarily back into use until property prices increase
Decision	

Problem	**Options**
A major service area, relating to a statutory responsibility of the organisation is to date overspent by £2million, on a budget of £12million for the year. Overspending in this area has been a major cause of the organisation's deficits for the last 3 years. The position has to be rectified	(a) Fund overspend from reserves and from next year ensure budgets are set from a zero base, and truly reflect the necessary expenditure (b) Calculate the expected outturn and the total expected overspend for the year. Cut expenditure on other non statutory services to fund overspends. Revise content of service to minimum level for future years so as to reduce expenditure (c) Take personal responsibility for this budget and gain a real understanding of why budget overspends are occurring. Accept the reality of another deficit year, but ensure strong control introduced for the future
Decision	

Problem	**Options**
Outstanding debtors are currently £35million, which is £5million more than target. This has lead to an overdraft of £3million, which is the limit currently available to the organisation. The position appears to be deteriorating rather than improving	(a) Implement a stronger credit control and collection policy, outsourcing if necessary (b) Negotiate a new overdraft limit with existing bankers or change banks (c) Introduce incentives for advance payments, such as discounts, charge reductions, and so on

Decision

Problem	**Options**
A piece of land for which planning has been granted for the development of housing is to be sold, however, the highest bidder is likely to be a private developer for luxury apartments and not the social housing sector, for which there is a great need in the area. A substantial profit on sale could be realised (up to £10million) depending on the selected purchaser	(a) Take the highest bidder in order to maximise profit and build reserves/fund overspends (b) Initiate a partnership between the private and social housing sector to allow for some social housing as part of the development, whilst maintaining a high bid price (c) Ensure social housing provision is part of the bid criteria, regardless of the impact this may have on the bid price
Decision	

Suggested solution is on page 139