The Chartered Institute of Public Finance & Accountancy

THE CIPFA FINANCIAL MANAGEMENT CODE

[Consultation Version]

the people in public finance

The CIPFA Financial Management Code

Objectives

The CIPFA Financial Management Code (CIPFA FM Code) is designed to support good practice in financial management and to assist local authorities in demonstrating their financial sustainability. The CIPFA FM Code therefore sets the standards of financial management for local authorities.

The Code is based on a series of principles supported by specific standards and statements of practice which are considered necessary to provide the strong foundation to:

- Financially manage the short, medium and long term finances of a local authority;

- manage financial resilience to meet foreseen demands on services; and

- financially manage unexpected shocks in their financial circumstances.

The Code is consistent with other successful CIPFA codes and statements in being based on principles rather than prescription. Each local authority (and those bodies designated to apply the Code) must demonstrate that the requirements of the Code are being satisfied. Demonstrating this compliance with the CIPFA FM Code is a collective responsibility of elected members, the Chief Finance Officer and their professional colleagues in the leadership team.

Significantly, the CIPFA FM Code builds on the success of the CIPFA Prudential Code which requires local authorities to demonstrate the long term financial sustainability of their capital expenditure and associated borrowing. With this success came new financial freedoms to make local decisions on matters that had hitherto been subject to central government control. The FM Code should not be considered in isolation and accompanying tools, including the use of objective quantitative measures of financial resilience, should form part of the suite of evidence to demonstrate sound decision-making.

The CIPFA FM Code has sought therefore to rely on the local exercise of professional judgement backed when appropriate by peer review.

The Applicability of the CIPFA Financial Management Code

1. CIPFA's intention is that the CIPFA Financial Management Code (CIPFA FM Code) will have the same scope as the Prudential Code for Capital Finance in Local Authorities (CIPFA, 2017) which promotes the financial sustainability of local authority capital expenditure and associated borrowing. So, although the CIPFA FM Code does not have legislative backing, it applies to all local authorities, including police, fire, combined and other authorities which:

   - in England and Wales are defined in legislation for the purposes of Part 1 of the Local Government Act 2003
   - in Scotland are defined in legislation for the purposes of Part 7 of the Local Government in Scotland Act 2003, or to the larger bodies (such as Integration Joint Boards) to which Section 10 of this Act applies, and
   - in Northern Ireland are defined in legislation for the purposes of Part 1 of the Local Government Finance Act (Northern Ireland) 2011.

2. In addition to its alignment with the Prudential Code for Capital finance in Local Authorities (CIPFA 2017), the CIPFA FM Code also has links to the Treasury Management in the Public Sector Code of Practice and Cross Sectoral Guidance Notes, (CIPFA 2017) and the annual Code of Practice on Local Authority Accounting in the United Kingdom. In this way the CIPFA FM Code supports authorities by re-iterating in one place the key elements of these statutory requirements.

3. The CIPFA FM Code is also further supported by statutory requirement, expressed in a different manner across the different jurisdictions of the United Kingdom, for all local authorities to have sound financial management;

   - Section 151 of the Local Government Act 1972 requires that every local authority in England and Wales should "... make arrangements for the proper administration of their financial affairs and shall secure that one of their officers has responsibility for the administration of those affairs".

   - Section 95 of the Local Government (Scotland) Act 1973 substantially repeats these words for Scottish authorities.

   - In Northern Ireland, section 54 of the Local Government Act (Northern Ireland) 1972 requires that "a council shall make safe and efficient arrangements for the receipt of money paid to it and the issue of money payable by it and those arrangements shall be carried out under the supervision of such officer of the council as the council designates as its Chief Finance Officer".

4. CIPFA's judgement is that compliance with the CIPFA FM Code is necessary for local authorities to demonstrate that they are meeting these important legislative requirements.

5. This legislation also makes sound financial management ultimately the responsibility of the Chief Finance Officer. With these responsibilities come obligations which are addressed in Section 1 of this Code. In England and Wales these responsibilities are further reinforced by Section 114 of the Local Government Finance Act 1988 which

requires the Chief Finance Officer to report to all the authority's councillors if there is or is likely to be unlawful expenditure or if expenditure in the year (including forecasted expenditure) is likely to exceed resources (including borrowings).

6. Section 114 does not apply to Scotland – instead the requirement to set a council tax which ensures a balanced budget is established in s93 (3) of the Local Government Finance Act 1992. In Northern Ireland, the equivalent duty – whilst not specified in statute – would rest with the authority's Chief Finance Officer in keeping with the statutory responsibility under section 54 of the Local Government Act (Northern Ireland) 1972.

7. In addition to the requirements of primary legislation and associated CIPFA Codes, an authority's prudent and proper financial management is informed by a framework of professional codes of practice and guidance, including

    - CIPFA Statements of Professional Practice (SOPP) (including ethics)
    - The CIPFA Statement of the Role of the Chief Financial Officer
    - The CIPFA Statement on the Role of the Chief Financial Officer in Local Government
    - CIFFA Statement on the Role of the Chief Finance Officer of the Police and Crime Commissioner and the Chief Finance Officer of the Chief Constable

    These statements are incorporated and, where necessary, elaborated in this CIPFA FM Code.

8. CIPFA considers the application of the CIPFA FM Code to be a professional responsibility of all its members, regardless of their role in the financial management process. More specifically, the FM Code clarifies CIPFA's understanding of how CFOs should satisfy their statutory responsibility for good financial administration. The responsibilities of the Chief Finance Officer are both statutory and professional. Notwithstanding these specific expectations of CIPFA members, the primary purpose of the CIPFA FM Code is to establish how the Chief Finance Officer – regardless of whether or not they are a CIPFA member – should demonstrate that they are meeting their statutory responsibility for sound financial administration.

9. CIPFA believes that this FM Code merits the type of statutory backing given to some of other CIPFA Codes and furthermore there is support for this approach within local government and its stakeholders. Equally, however, CIPFA recognises that such backing demands enabling primary legislation which at present has not been identified. CIPFA will continue to work with the jurisdictions of the different parts of the United Kingdom to provide statutory backing to the Code. At present it is difficult to envisage circumstances in which the absence of statutory backing for the FM Code would provide a reason for non-compliance.

<u>Application Date</u>

10. Local authorities are required to apply the requirements of the CIPFA FM Code with effect from 1st April 2020. This means that to enable the 2020/21 budget to have been prepared in compliance with the Code significant elements of the CIPFA FM Code will have to be adopted before April 2020. Authorities will need to ensure that their governance and financial management style are fit in advance for this purpose. Additionally, they will have had to have initiated the longer term financial planning demanded by this Code.

The CIPFA Statement of Principles of Good Financial Management

11. The CIPFA FM Code applies a principle-based approach. It does not prescribe the financial management processes that local authorities should adopt. Instead, this Code requires that a local authority demonstrate that its processes satisfy the principles of good financial management for an authority of its size, responsibilities and circumstances. Good financial management is proportionate to the risks to the authority's financial sustainability posed by the twin pressures of scarce resources and the rising demands on services. The FM Code identifies these risks to financial sustainability and introduces an overarching framework of assurance which builds on existing best practice but which for the first time sets explicit standards of financial management.

12. The underlying principles that inform the CIPFA FM Code have been developed in consultation with senior practitioners from local authorities and associated stakeholders. The principles have been designed to focus on an approach which will assist in determining whether, in applying standards of financial management a local authority is financially sustainable.

    - **Organisational leadership - demonstrating a clear strategic direction based on a vision in which financial management is embedded into organisational culture**
    - **Accountability - based on medium term financial planning which drives the annual budget process supported by effective risk management, quality supporting data and whole life costs**
    - **Financial management is undertaken with transparency at its core using consistent, meaningful and understandable data, reported frequently with evidence of periodic officer action and elected member decision making**
    - **Adherence to professional Standards is promoted by the leadership team and is evidenced.**
    - **Sources of assurance are recognised as an effective tool mainstreamed into financial management and includes political scrutiny and the results of both external audit, internal audit and inspection.**
    - **The long term sustainability of local services is at the heart of all financial management process and is evidenced by prudent use of public resources.**

13. The CIPFA FM Code has been developed and tested in partnership with a range of different types of local authorities. Given the diversity of UK local government, it is not however possible (or desirable) for the Code to anticipate all eventualities. If any doubt arises as to whether or how the CIPFA FM Code should be applied, then reference should be made to these Principles of Good Financial Management to establish whether the proposed financial management practice is acceptable. A

financial management practice that conflicts with one or more of these principles will not be acceptable practice even if not explicitly ruled out by the Financial Management Standards contained in the CIPFA FM Code.

The Financial Management Standards.

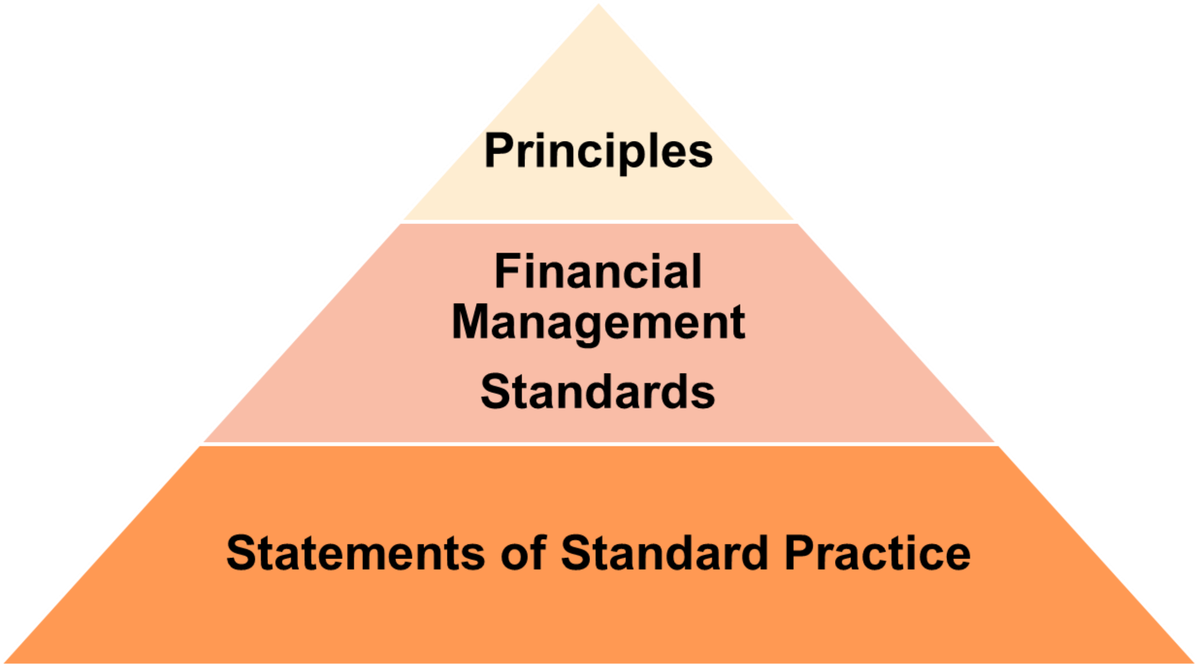
14. It is the duty of each local authority to adhere to the principles of financial management. To enable authorities to test their conformity with the CIPFA Principles of Good Financial Management, the CIPFA FM Code translates these principles into

    - Financial Management Standards; and
    - Statements of Standard Practice.

    These Financial Management Standards and supporting Statements of Standard Practice provide the flexibility necessary for the CIPFA Principles of Good Financial Management to have practical application according to the different circumstances of each authority.

The Structure of the Code

15. The CIPFA Financial Management Standards are presented and explained in Sections 1 to 7 of the FM Code. These sections also introduce the Statements of Standard Practice which are shown with the FM Standards in the schedule on page 52 to 57. The principles set out in paragraph 12 are supported by defined financial management standards, the adherence to which will be by application of statements of standard practice. There is therefore a clear hierarchy. All principles require to be applied and the statements of standard practice set the minimum requirement to demonstrate adherence to the Code

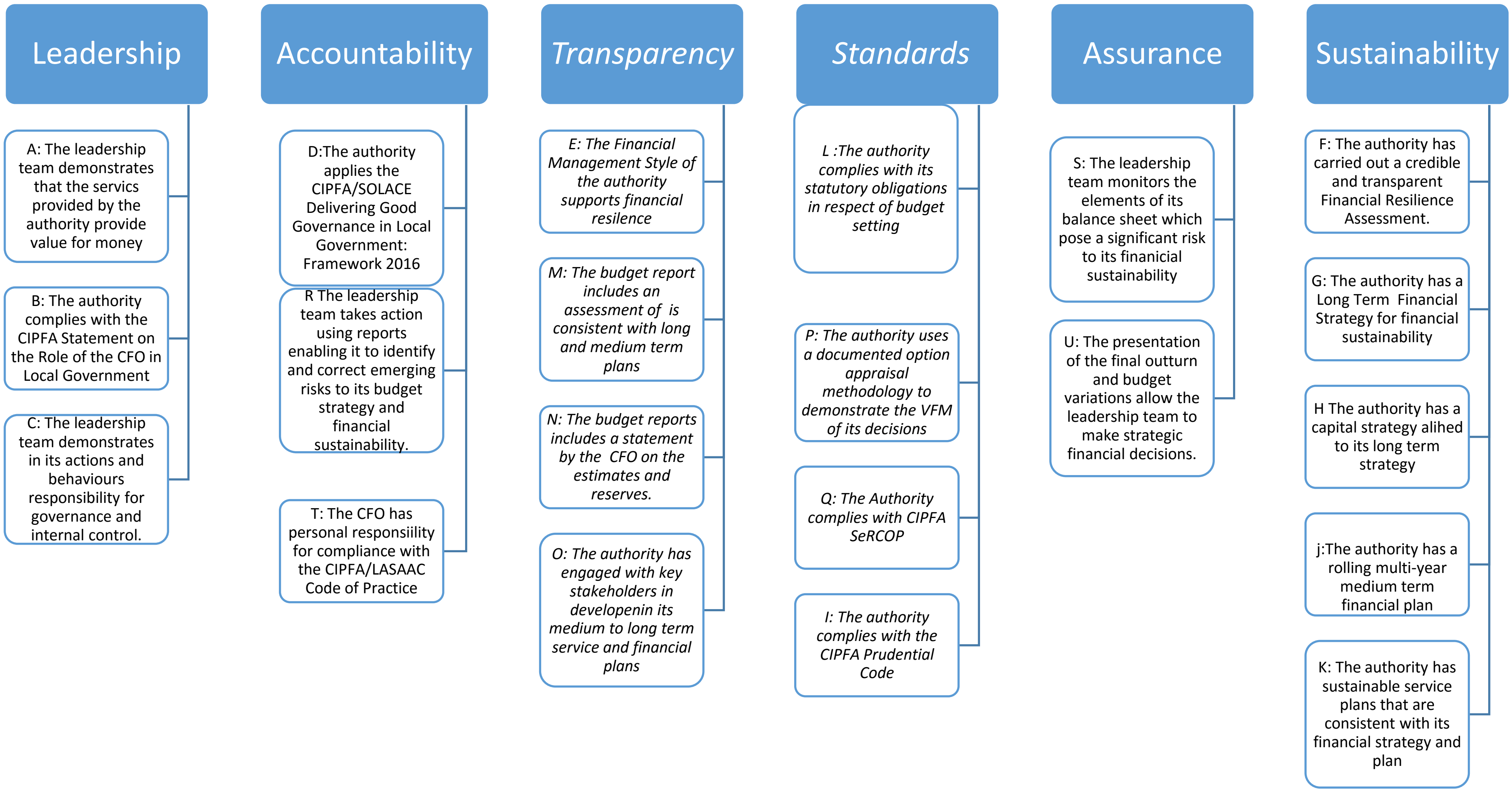


FM Standard Reference	**CIPFA Financial Management Standards**
	Section 1 The Responsibilities of the Chief Finance Officer and Leadership Team
A	The leadership team demonstrates that the services provided by the authority provide value for money.
B	The authority complies with the CIPFA Statement on the Role of the Chief Finance Officer in Local Government
	Section 2 Governance and Financial Management Style
C	The leadership team demonstrates in its actions and behaviours responsibility for governance and internal control.
D	The authority applies the CIPFA/SOLACE Delivering Good Governance in Local Government: Framework (2016)
E	The Financial Management Style of the authority supports financial sustainability
	Section 3 Long to Medium Term Financial Management
F	The authority has carried out a credible and transparent Financial Resilience Assessment
G	The authority has a Long Term Financial Strategy for financial sustainability.
H	The authority has a capital strategy aligned to its long term financial strategy
I	The authority complies with the CIPFA Prudential Code for Capital Finance in Local Authorities
J	The authority has a rolling multi-year Medium Term Financial Plan
K	The authority has sustainable service plans that are consistent with its long term financial strategy and the medium term financial plan
	Section 4 The Annual Budget
L	The authority complies with its statutory obligations in respect of the budget setting process.
M	The budget report includes an assessment of its consistency with the current medium term financial plan and long term financial strategy.
N	The budget report includes a statement by the Chief Finance Officer on the robustness of the estimates and a statement of the adequacy of the proposed financial reserves.
	Section 5 Stakeholder Engagement and Business Plans
O	The authority has engaged with key stakeholders in developing its long term financial strategy, medium term financial plan and annual budget.
P	The authority uses a documented option appraisal methodology to demonstrate the VFM of its decisions
Q	The authority applies the principles contained in the CIPFA Service Reporting Code of Practice and utilises appropriate costing techniques in the development of business cases.
	Section 6 Monitoring Financial Performance

R	The leadership team takes action using reports enabling it to identify and correct emerging risks to its budget strategy and financial sustainability.
S	The leadership team monitors the elements of its balance sheet which pose a significant risk to its financial sustainability.
	Section 7 External Financial Reporting
T	The Chief Finance Officer has personal responsibility for ensuring that the statutory accounts provided to the local authority comply with the Code of Practice on Local Authority Accounting in the United Kingdom.
U	The presentation of the final outturn figures and variations from budget allow the leadership team to make strategic financial decisions.

The following diagram maps the CIPFA FM Standards onto the Principles of Financial Management.

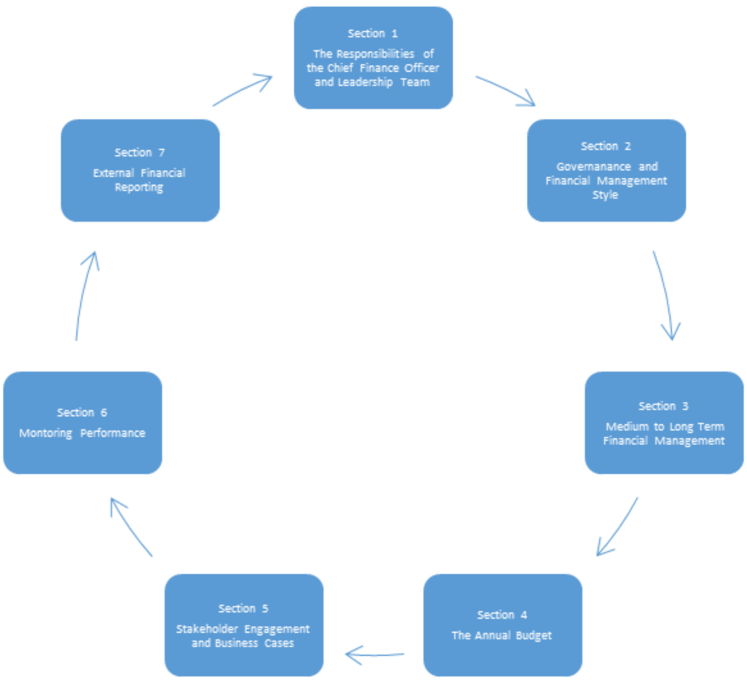
Mapping of CIPFA summarised Financial Management Standards onto CIPFA Principles of Good Financial Management (DRAFT)



16. Sections 1 and 2 of the FM Code address important contextual factors which need to be addressed in the first instance if sound financial management is to be possible. The first deals with the responsibilities of the Chief Finance Officer and leadership team; the second with the authority's governance and financial management style From a professional perspective, these factors are the most challenging to codify as they largely concern 'soft skills' and behaviours. Nonetheless, it will be seen that even here there are recognised standards of best practice which authorities must adopt if their organisational culture is to be favourable for sound financial management. A 'tick box' compliance with these standards alone will not however be sufficient if they do not promote the behaviours necessary for good financial management.

17. The remaining sections 3 to 7 address the requirements of the financial management cycle starting in section 3 with the need for a long term approach to the evaluation of financial sustainability. To make well informed decisions all these elements of the cycle need to be fit for purpose. The development of a high quality long term financial strategy will not itself promote financial sustainability if, for example, the authority's annual budget setting (section 4), stakeholder engagement and business cases (section 5) and performance monitoring arrangements (section 6) are inadequate. The cycle is completed by section 7 which shows how high quality financial reporting provides the basis for the financial management cycle to restart on a sound basis.

The Virtuous Financial Management Cycle



18. CIPFA's expectation is that authorities will have to comply with all the Financial Management Standards if they are to demonstrate compliance with the FM Code. This compliance will typically but not always be demonstrated by documenting

compliance with the Statements of Standard Practice which underpin each of the CIPFA Financial Management Standards. It is most important that practitioners recognise that while compliance with the CIPFA Financial Management Standards is obligatory for compliance with the Code, the Code is not prescriptive about how this compliance is achieved. The Statement of Standard Practice are, as their name suggests, practices that are often to be found across local authorities, but CIPFA recognises that they are not universal and so are not prescribed by this Code.

19. As high level statements of proper practice, the overarching CIPFA Financial Management Standards do apply to the police service. CIPFA recognises, however, that this service has in some respects different practices from other local authorities. As a consequence it will need to demonstrate compliance with some of these Financial Managements Standards by alternatives to the Statements of Standard Practice contained in this Code. In doing this they would be using on a more widespread basis the flexibility offered to all authorities in the practices used to comply with the Financial Management Standards.

20. Some of these Statements of Standard Practice refer to current legislative, regulatory or professional standards. These are likely to change over time, but this will result only in a change in how compliance with the CIPFA FM Standard is demonstrated and not a change in the Financial Management Standards. The distinction between Financial Management Standards and Statements of Standard Practice should enable the essential demands of the CIPFA FM Code to have longevity even though changes can be expected in some of the detailed application.

21. CIPFA may issue additional or replacement Statements of Standard Practice to support and clarify application of the FM Code. These statements of standard practice represent the minimum required to achieve compliance with this Code. Local authorities can develop their own local statements of standard practice and are encouraged to do so.

22. The CIPFA FM Code also uses Statements of Standard Practice in recognition of the need for the practical application of (some) Financial Management Standards to be guided by proportionality. It is appropriate for different financial management approaches to apply to high value/high risk items that alone may determine the financial sustainability of the organisation as distinct from low value/low risk items. In satisfying the demands of the Financial Management Standards it may be appropriate to apply different standard practices according to the scale and risks of each category of income or expenditure. The intention is that authorities demonstrate a rigorous approach to the assessment and mitigation of risk so that financial management expertise is deployed effectively given the circumstances faced by the authority.

23. Nonetheless, in acknowledging the need for proportionality in applying some aspect of the CIPFA FM Code, an authority still needs to recognise that when aggregated, a failure to manage individual low value/low risk items may still threaten financial sustainability. The CIPFA FM Code seeks to promote the good financial management of the standard, typical or familiar local authority activities just as much as it promotes the good financial management of the unusual, exception and unfamiliar. Essentially, the CIPFA FM Code recognises that getting the routine business right is crucial for good financial management.

24. So while flexibility in the application of the Statements of Standard Practice is appropriate, any departure from the Statements of Standard Practices must be demonstrated to still leave the authority able to satisfy both the Financial Management Standards and comply with the overarching Financial Management Principles. CIPFA's expectation is that CIPFA FM Code should be applied in this way on a 'comply or explain' basis. If necessary this requirement could be formalised by including it within the requirement of the Annual Government Statement – as has been done for the *CIPFA Statement on the Role of the Chief Finance Officer in Local Government*.

Section 1: The Responsibilities of the Chief Finance Officer and Leadership Team

25. Local authorities in the United Kingdom use different democratic models. While the committee and the cabinet system is the most common there are also a number of direct elected mayors in England. Regardless of the detail, responsibility for corporate financial sustainability rests with those responsible for making executive decisions with the support of their professional advisors. The FM Code follows the practice of other CIPFA Codes in referring to this collective group of elected member and officers with this collective financial responsibility as the leadership team. In local authorities, therefore, the concept of the 'leadership team' will include executive committees, elected mayors, portfolio holders with delegated powers and other key committees of the authority. In the police service this leadership is provided by Police and Crime Commissioners and Chief Constables.

26. While the legislative context differs across the different jurisdictions of the United Kingdom, all local authorities must deliver value for money. So, while Financial Management Standard A is not supported by any specific Statements of Standard Practice, the need to comply with it should inform the application of the other Financial Management Standards and Statements of Standard Practice in the FM Code.

Financial Management Standard A **The leadership team demonstrates that the services provided by the authority provide value for money.**

<u>The Role of the Chief Finance Officer</u>

27. The statutory role of the Chief Finance Officer (CFO) is a distinctive feature of local government in the United Kingdom. This role cannot however be performed in isolation but only with the support of the other members of the leadership team. The leadership team must recognise that responsibility for the financial management of the authority does not rest with the Chief Finance Officer alone, but with the actions of the leadership team both collectively and individually as elected members and senior officers.

28. Equally, the Chief Finance Officer must ensure that they fulfil their personal legal and professional responsibilities in the public interest and in recognition of the other statutory service responsibilities of the authority. A situation in which the Chief Finance Officer is forced to act in isolation is characteristic of authorities in which financial management had failed and financial sustainability is threatened.

29. In the leadership team the Chief Finance Officer must provide timely, relevant and reliable financial advice, in accordance with the law and professional standards. To support Chief Finance Officers and authorities by setting out its understanding of the role, CIPFA has issued a *Statement on the Role of the Chief Finance Officer in Local Government*.

Financial Management Standard B

The authority complies with the CIPFA Statement on the Role of the Chief Financial Officer in Local Government

30. For the purposes of the CIPFA FM Code the CIPFA Statement on the Role of the Chief Finance Officer of the Police and Crime Commissioner and the Chief Finance Officer of the Chief Constable (2012) should be substituted for references to the CIPFA *Statement on the Role of the Chief Financial Officer in Local Government*.

31. CIPFA's statement on the role of the Chief Finance Officer in Local Government describes the roles and responsibilities of the Chief Finance Officer. It sets out how the requirements of legislation and professional standards should be fulfilled by the Chief Finance Officer as they carry out their duties. The statement is designed to assist those carrying out the role to meet its specific responsibilities while at the same time reiterating CIPFA's statement of professional practice with which all CIPFA members are required to comply.

32. The Statement also requires that if different organisational arrangements are adopted the reasons should be explained publicly in the authority's Annual Governance Report, together with how these deliver the same impact. Compliance with the CIPFA FM Code will equally demand this disclosure be made to explain how the Statement of Standard Practice is being met.

33. To enable authorities to demonstrate compliance with the CIPFA Statement on the Role of the Chief Finance Officer in Local Government, its key elements are presented below as Statements of Standard Practice. In doing so the FM Code does not change the role of the Chief Finance Officer from that set out in the existing statement, but it presents its elements in a format that allows a systematic assessment of an authority's compliance.

34. CIPFA considers that it is important for the Chief Finance Officer to be at the 'top table' with a status at least equivalent to other members. This status must be respected in practice and not be simply a theoretical status based on a position in the organisation. This increases awareness of the importance of financial planning and closely aligns financial and wider business planning. While performing this key role within the leadership team CFOs also have a responsibility to advise those members not in executive or leadership roles.

Statement of Standard Practice B1

The Chief Finance Officer in a public service organisation is a key member of the leadership team, helping it to develop and implement strategy and to resource and deliver the organisation's strategic objectives sustainably and in the public interest

[From CIPFA: The Role of the Chief Financial Officer in Local Government (2016) p 7]

35. The statutory guidance issued by the Secretary of State under the 2000 Local Government Act (England and Wales) advises that local authorities will need to ensure that the Chief Finance Officer and the monitoring officer have access as necessary to meetings and papers and that members must consult with him/her

regularly. There is no equivalent legislative requirement in Scotland or Northern Ireland, but the guidance is equally relevant as a statement of good practice.

> *Statement of Standard Practice B2*
>
> *The Chief Finance Officer must be actively involved in, and able to bring influence to bear on, all material business decisions to ensure immediate and longer term implications, opportunities and risks are fully considered, and alignment with the organisation's financial strategy*
>
> *[From CIPFA: The Role of the Chief Financial Officer in Local Government (2016) p 7]*
>
> *Organisations which are required to explain (rather than comply) should set out clearly how the associated risks will be managed and demonstrate notification of the risks to the political leadership.*

36. The Chief Finance Officer should support members of the leadership team in seeking to match their financial competences with those necessary for their roles to be performed effectively. This would be done proportionately, with the focus being on those roles which carried the greatest financial responsibilities and hence financial management risk. Ultimately, however, the performance of the elected members and their professional advisers is not the responsibility of the Chief Finance Officer but of the political process and HR policies respectively. So, while the statutory role of the Chief Finance Officer must be recognised, at the same time all members of leadership team must recognise their own responsibilities in support of good financial management.

> Statement of Standard Practice B3
>
> *The Chief Finance Officer must lead the promotion and delivery by the whole organisation of good financial management so that public money is safeguarded at all times and used appropriately, economically, efficiently and effectively.*
>
> *[From CIPFA: The Role of the Chief Financial Officer in Local Government (2016) p 7]*
>
> *The Chief Finance Officer should regularly review the skillsets of elected members and all officers with budget/financial management responsibility and ensure appropriate support is provided.*

37. The wider finance function in an organisation encompasses those staff and systems deployed in processing financial transactions, achieving compliance and providing interpretation and advice regarding the financial situation outlook. Many of these functions will be performed by staff over whom the Chief Finance Officer does not exercise management control so in promoting sound financial management the Chief Finance Officer will need to reply on the commitment of other senior managers.

38. Good financial management requires technical professional knowledge, commercial and political awareness and 'soft' people orientated skills. The finance profession is in both the private and public sectors one in which professional and technical expertise is demonstrated by a full professional accounting or auditing qualification as well as, for some specialised roles, a credible technical qualification. A local authority should therefore ensure that its mix of qualified to unqualified finance staff gives it assurance that it has access to the right mix and level of financial skills.

Statement of Standard Practice B4

The Chief Finance Officer must lead and direct a finance function that is resourced to be fit for purpose

[From CIPFA: The Role of the Chief Financial Officer in Local Government (2016) p 7]

The Chief Finance Officer should regularly review the skill sets of all finance staff with senior budget/financial management responsibility and ensure ongoing appropriate support is provided.

The ratio of qualified staff as a proportion of total finance staff ensures that the finance function has the necessary financial competence.

39. One cost effective way of assessing costs and performance is by benchmarking, of which the ratio of qualified staff is an example. A more thorough review may be necessary to gain a more nuanced view of the qualitative performance of an authority's finance function. This could be undertaken as part of a wider review of the authority's financial management (see Section 2 of this Code).

40. While statute requires that the Chief Finance Officer is professionally qualified, this is evidently insufficient unless complemented by suitable experience and supported by continuing professional development. The Chief Finance Officer must be a highly experienced finance practitioner who is able to lead, coach, inspire and empower others. Additionally the Chief Finance Officer must be a strategic thinker able to operate at the highest levels both internally and externally.

Statement of Standard Practice B5

The Chief Finance Officer must be professionally qualified and suitably experienced.

[From CIPFA: The Role of the Chief Financial Officer in Local Government (2016) p 7]

The Chief Finance Officer must be able to demonstrate adherence to professional CPD requirements on an annual basis

41. Importantly, as a professionally qualified accountant the Chief Finance Officer should also have regard to their own professional body's Code of Ethics as well as that produced by International Ethics Standards Board for Accountants (IESBA) on behalf of the International Federation of Accountants (IFAC). CIPFA's interpretation of these responsibilities is that not only must the Chief Finance Officer demonstrate the highest standards of ethics but he or she must actively promote these standards across the local authority.

42. In the context of the CIPFA FM Code, this is especially relevant because sound financial management relies on the integrity of all those involved. The financial implications of alternative options needs to be evaluated and presented objectively. Unpalatable information should not be hidden because they bring with it potentially unwelcome consequences for those involved. Similarly, encouraging personal responsibility for budgetary control and wider management should not be done in a manner that creates perverse incentives that discourage the telling of bad news.

Statement of Standard Practice B6 *The Chief Finance Officer should promote the highest standards of ethical behaviour in the conduct of financial management.* *Professionally qualified staff should demonstrate an ongoing commitment to the principles of objectivity, integrity professional behaviour, professional competence, due care and confidentiality.*

43. The Chief Finance Officer may not personally have detailed technical knowledge of all aspects of local government finance, but does need to have personal credibility when giving advice to the leadership team. This means that Chief Finance Officer should have in place a mechanism which ensures that he/she is properly advised on all aspects of local government finance at all times.

Statement of Standard Practice B7 *To enable financially informed decision making:* *The Chief Finance Officer should be able to provide the leadership team with sound advice on the key principles of local government finance; and* *The Chief Finance Officer should be able to demonstrate a sound system which ensures the authority has access to high standards of technical financial advice.*

44. While the whole leadership team has responsibility for compliance with the CIPFA Prudential Code for Capital Finance in Local Authorities (2017 Edition), the Prudential Code does include as specific responsibility on the Chief Finance Officer in respect of the capital strategy and associated treasury management.

Statement of Standard Practice B8 *The Chief Finance Officer should report explicitly on the affordability and risk associated with the capital strategy and where appropriate have access to specialised advice to enable them to reach their conclusions.* *The Prudential Code for Capital Finance in Local Authorities 2017 Edition Page 13*

45. There are many different routes to the top finance role, so it is possible that Chief Finance Officers will not have encountered every aspect of local government finance during their earlier professional career. This is especially the case in respect of treasury management and the Local Government Pension Scheme (LGPS) which are typically the immediate responsibility of highly technical expert practitioners while at the same time being critical to the long term financial resilience of the authority.

46. The *CIPFA Treasury Management in The Public Services, Guidance Notes For Local Authorities Including Police Forces And Fire And Rescue Authorities (2018 Edition)* places specific responsibilities on the Chief Finance Officer

Statement of Standard Practice B9

The Chief Finance Officer must establish the reporting and monitoring processes, and integrate the treasury management indicators into the overall financial planning process.

CIPFA Treasury Management in The Public Services, Guidance Notes for Local Authorities including Police Forces and Fire and Rescue Authorities (2018 Edition) p9

47. CIPFA has also produced detailed guidance which includes a precise specification of the knowledge and skills relating to pensions that should be secured by a Chief Finance Officer for a Local Government Pension Scheme administering authority.

Statement of Standard Practice B10

The Chief Finance Officer of Local Government Pension Scheme (LGPS) administering authorities satisfies the requirements of the CIPFA Code of Practice on Public Sector Pensions Finance Knowledge and Skills (2013 edition)

48. This first section of this Code has stressed the responsibilities of the Chief Finance Officer. He or she is not alone responsible for financial management. It is for the leadership team to ensure that the authority's governance arrangements and style of financial management promote financial sustainability. These issues are addressed in the next section of the CIPFA FM Code.

Section 2: Governance and Financial Management Style

49. Without good governance a local authority cannot make the changes necessary for it to remain financially sustainable. So financial sustainability must be underpinned by the robust stewardship and accountability to be expected of public bodies. Good governance gains the trust of taxpayers and other funders by giving them confidence that money is being properly spent. Good governance also encourages better informed and longer-term decision making and as a consequence is essential for good financial management.

50. All those with a role in the financial management process need to maintain high values of integrity, transparency and accountability to the public, who have an interest in knowing how their taxes are being spent. This is especially the case when different decisions are made to restrict access to non-statutory services by techniques such as queuing and rationing. Political judgement is also needed to resolve any potential tensions between social outcomes (e.g. anti-poverty policies) and administrative efficiency (e.g. maximising income collection). An effective leadership team is one in which the primacy of the political process is wedded effectively to a recognition of the demands which the statutory framework and good practice place on all those in local government.

Good Governance

51. In local authorities the concept of the 'leadership team' will include executive committees, elected mayors, portfolio holders with delegated powers and other key committees of the authority. Responsibility for good governance rests with this leadership team, even though in practice it is delivered through a proper scheme of delegation that ensures that frontline responsibility for internal and financial control starts with those who have management roles. This delegation ensures that those responsible for the delivery of services are also explicitly held responsible for the financial management of the associated expenditure and income. Nonetheless, it is for the leadership team to demonstrate that the authority always meets exacting standards of probity and accountability and demonstrable efficiency in the use of public resources.

52. The Chief Finance Officer is not the only professional adviser on the leadership team that has specific statutory responsibilities for good governance. The Head of Paid Service (in practice the Chief Executive) is responsible for the proper recruitment and organisation of a local authority's staff. The Monitoring Officer has the specific duty to ensure that the Council, its officers, and its elected members maintain the highest standards of conduct in all they do. [1]

53. Good governance is evidenced by actions and behaviours rather than only formal documentation and processes. The tone and action at the top are critical in this respect, and rest with the leadership team – including both senior officers and elected members - and not just the Chief Finance Officer. A successful leadership

[1] The legal basis of the Head of Paid Service's role is found in Section 4 of the Local Government & Housing Act 1989 and the monitoring officer Section 5 of the same Act.

team has a culture of constructive challenge that excludes an optimism bias in favour of a realism bias, built on rigorous examination of goals, underlying assumptions and implementation plans.

54. The Public Standards Committee has set out 'Seven Principles of Public Life' which it believes should apply to all in the public service. These are:

- Selflessness: Holders of public office should act solely in terms of the public interest. They should not do so in order to gain financial or other benefits for themselves, their family or their friends.
- Integrity: Holders of public office should not place themselves under any financial or other obligation to outside individuals or organisations that might seek to influence them in the performance of their official duties.
- Objectivity: In carrying out public business, including making public appointments, awarding contracts, or recommending individuals for rewards and benefits, holders of public office should make choices on merit.
- Accountability: Holders of public office are accountable for their decisions and actions to the public and must submit themselves to whatever scrutiny is appropriate to their office.
- Openness: Holders of public office should be as open as possible about all the decisions and actions that they take. They should give reasons for their decisions and restrict information only when the wider public interest clearly demands.
- Honesty: Holders of public office have a duty to declare any private interests relating to their public duties and to take steps to resolve any conflicts arising in a way that protects the public interest.
- Leadership: Holders of public office should promote and support these principles by leadership and example.

55. The last of the Nolan Principles is especially relevant to the leadership team as it especially important that they demonstrate leadership and example in their standards of behaviour.

Financial Management Standard C

The leadership team demonstrates in its actions and behaviours responsibility for governance and internal control.

56. The *CIPFA/IFAC International Framework: Good Governance in the Public* Sector (Annex A to this FM Code) is intended to encourage better service delivery and improved accountability by establishing a benchmark for aspects of good governance in the sector. By international standards, local government in the United Kingdom is distinguished by high standards of governance. Citizens expect financial accountability, press and parliamentary scrutiny, integrity and the absence of

corruption. These expectations are largely met, but local authorities should guard against complacency.

57. The application of this CIPFA/IFAC International Framework in the context of UK local government is reinforced by specific regulatory requirements and sector specific guidance. The *CIPFA/SOLACE Delivering Good Governance in Local Government: Framework (2016 Edition)* supports local authorities in developing and maintaining their own codes of governance and discharge their accountability for the proper conduct of business. Its statements of principles are in Annex B of this FM Code

> ***Financial Management Standard D***
>
> ***The authority applies the CIPFA/SOLACE Delivering Good Governance in Local Government: Framework (2016)***

58. This CIPFA/SOLACE Framework recommends that the review of the effectiveness of the system of internal control that local authorities in England, Wales Scotland and Northern Ireland are required to undertake by their respective Accounts and Audit Regulations should be reported in an Annual Governance Statement (AGS).

Audit

59. It is primarily the responsibility of the leadership team to maintain the financial sustainability of the authority. External auditors can however be expected to request evidence on, and will draw attention to any material concerns, regarding the financial sustainability of the authority. It is the role of the audit committee to ensure that this independent feedback on the soundness of financial management is made known to and addressed by the leadership team.

> Statement of Standard Practice D1
>
> The authority maintains an effective audit committee

> *Statement of Standard Practice D2*
>
> *The audit committee receives and monitors the implementation of internal and external audit recommendations. When threats to the financial sustainability of the authority are identified by auditors the audit committee should ensure that the recommendations are communicated to the leadership team and that the committee are informed of the effectiveness of the leadership team's response.*

60. The mandatory internal audit Standards for local government in the UK are the *Public Sector Internal Audit Standards (PSIAS)*, incorporating the Mission, Core Principles, Definition of Internal Auditing and the Code of Ethics as well as the Attribute and Performance Standards. The mission of internal audit which is embodied in these mandatory internal audit standards is a wide-ranging one: 'to enhance and protect organisational value by providing risk-based and objective assurance, advice and insight.' This should extend to considering the risks to financial sustainability and working to protect the authority from them.

Statement of Standard Practice D3

The authority has a PSIAS conformant internal audit function

Financial Management Style

61. The financial management challenges faced by many local authorities are unprecedented in recent history and show no signs of easing. This is significant because it means that different styles of financial management are necessary. Financial sustainability will not be achieved by continuing with the behaviours of the past since these will not meet the demands of the present and the possibly even more challenging future. To remain financially sustainable authorities need to develop their financial management capabilities.

Financial Management Standard E

The Financial Management Style of the authority supports financial sustainability.

62. CIPFA believes that the strength of financial management within an organisation can be assessed by a hierarchy of three 'financial management (FM) styles':

- Delivering accountability
- Supporting performance
- Enabling transformation

63. These different styles are used in the CIPFA Financial Management Model to describe the different standards of financial management which may be found in local authorities. They represent a hierarchy in which success in enabling of transformation is only achieved by a financial management style which supports performance and which in turn delivers accountability. Once these basic foundations have been soundly established, in response to increasing risk authorities need to move up through a hierarchy of financial management styles. This is especially as risks have increased for many local authorities; on the one hand reduced expenditure leaves less margin for error while on the other hand in seeking to generate new income local

authorities take on unfamiliar risks.

[Diagram from CPA Australia - https://www.cpaaustralia.com.au/training-and-events/corporate-learning-solutions/public-sector-financial-management-model]

64. This hierarchy of financial management styles loosely maps onto the now deeply embedded recognition of the necessity for economy, efficiency and effectiveness to achieve value for money. In delivering accountability the finance team ensures that their authorities spend less and so achieve economy. In supporting performance the finance team works with the authority to spend well by maximising the output from goods or services and so achieves efficiency. Finally, in enabling transformation the finance team supports the effective use of public money.

Delivering accountability

65. Delivering accountability is the traditional stewardship role of finance. It addresses the regulatory and accountability requirements (such as the need for annual financial statements and an external audit) but with little direct involvement in the organisation's activities. While in itself this basic style of financial control is insufficient to meet the challenges now facing local authorities, it is a fundamental requirement that should not be neglected or trivialised. Using resources effectively is the responsibility of every manager charged with delivering local authority services.

66. Local authority financial management is not just about accountants keeping track of income and expenditure; managers need to take ownership of their budget responsibilities. The leadership team must have a culture of collective responsibility for financial matters. A symptom of financial weakness is significant break down in the existing system of budgetary control (for example, illustrated by poorly understood or unchallenged variances), its replacement by expenditure freezes and other crude ad hoc systems and *in extremis* the issuing of a Section 114 Notice.

Statement of Standard Practice E1

The organisation has an effective framework of financial accountability that is clearly understood and applied throughout, from the political leaders, elected members to directors, finance officers and front line service managers.

[Adapted from CIPFA FM Model]

Supporting performance

67. Having worked with colleagues to secure accountability, the role of finance professionals is to act as business partners by using their expertise to support operational managers. With devolved financial responsibilities the leadership and managers need to be financially literate and finance professionals need to contribute challenge, interpretation and advice.

Statements of Standard Practice E2

Finance teams and the organisation they support are actively committed to continuous improvement focused on efficient and effective delivery and organisational performance.

[Adapted From CIPFA FM Model]

Enabling transformation

68. The third, most advanced style of financial management, is required to ensure financial sustainability. Transformation involves a significant change in approach to an organisation's operating model, its technology, processes and/or service delivery, in order to deliver better outcomes and improve efficiency. These changes bring new challenges for the finance function as the objective is to achieve continuous improvement. Nonetheless, traditional public sector financial disciplines remain important.

Statement of Standard Practice E3

Enabling transformation: the finance team have input into strategic and operational plans taking into account proactive risk management, clear strategic directions and focus-based outcomes

[From CIPFA FM Model]

69. These need to be communicated and addressed by the leadership team. The leadership team must have a culture of collective responsibility for financial matters.

> *Statement of Standard Practice E4*
>
> *Managers understand they are responsible for delivering services cost effectively and are held accountable for doing so. Financial literacy is diffused throughout the organisation so that decision takers understand and manage the financial implications of their decisions.*
>
> *[From CIPFA FM Model]*

<u>*Peer and Critical Review*</u>

70. Each local authority has its own financial management style; many display excellent practices but all would benefit from a critical evaluation. A rigorous peer review is a good way of doing this; but while CIPFA advocates such peer review it does not mandate it. Nor does it mandate any specific approach except to note that it should be one that has credibility within the sector and its stakeholders. Where an authority has not been subject to a peer review it must demonstrate how it has assessed the effectiveness of its financial management and sought the benefits of new ideas and a different perspective.

> *Statement of Standard Practice E5*
>
> *The financial management of the authority has been critically evaluated.*

71. The leadership team should exercise judgement to determine when and how regularly its financial management should be critically evaluated. It would be essential in the event of systematic failure or after a period of rapid organisational change; but an incoming Chief Finance Officer may also use a critical evaluation to ensure compliance with the role’s statutory and professional responsibilities.

72. The first two sections of this Code have addressed the pre-conditions that must be satisfied for sound financial management. The following sections turn to the practical operation of the successive stages of the financial management cycle.

Section 3: Medium to Long Term Financial Management

73. While the statutory local authority budget process continues to be an annual process (Section 4 below) a longer term perspective is essential if local authorities are to demonstrate their financial sustainability. Progress had been made in promoting medium term financial planning, by for instance multi-year term financial settlements between local and central government. With the era of austerity this ceased and there is some evidence that financial planning timescales are shortening.

74. While consequence of this short-term financial planning is that many authorities have only specified how savings will be achieved for the next financial year and even some of these may be targets rather than firm plans. An important indicator of an excessively short term approach is the existence of 'still to be found' gaps in saving plans. Arguably these may reflect political reality, but equally they may reflect an inability to face unwelcome realities. A failure to plan ahead indicates a lack of strategic thinking and an unwillingness to address difficult issues such as the possibility of ceasing some non-statutory services or changes in the delivering of those to which the authority remains committed.

75. Short-termism runs counter to both sound financial management and sound governce. *CIPFA/SOLACE Delivering Good Governance in Local Government: Framework* (2016), which is incorporated into these CIPFA FM Standards, makes explicit in elaborating its Principle C that the 'long-term nature and impact of many of local government's responsibilities mean that it should define and plan outcomes so that these should be sustainable'.

76. This more strategic approach required by the FM Code is characterised by a distinction between those savings for which there is a clear delivery plan, those which have been agreed in principle but do not yet have a clear implementation plan and those that are simply ideas. Only the first should feature in the annual budget; and even the success (or failure) of these need to be tracked over the medium term if the lessons learnt are to inform decision making.

77. One of the strengths of UK local government is its diversity, with even authorities of the same size and type having a different organisational culture. It is this that allows a close relationship between local authorities and the communities which they serve. Its style of financial management should reflect, for example, its reliance on local tax income or scope to utilise additional grant or trading income. CIPFA does not believe however that the time horizon of local authority financial planning is determined by the time horizon of the financial support from central government.

78. Central government has encouraged the idea that local authorities can control their own financial destiny through measures such as promoting housebuilding and growing the local economy. CIPFA recognises that there are sharp contrasts in councils' inherent ability to take advantage of this approach since it has not always been backed up by a resources or operational freedoms. Nonetheless, the greater the uncertainty about future central government policy then the greater the need to demonstrate the long term financial resilience of the authority given the risks attached to its core funding.

Financial Resilience and Long Term Financial Strategy

79. If an authority has not tested and demonstrated its long term financial resilience then its financial sustainability remains an open question. Authorities must critically evaluate their financial resilience. It is possible that the existing strategy is financially sustainable, but this must still have been tested and demonstrated in a Financial Resilience Assessment.

80. In this Financial Resilience Assessment it is necessary to test the sensitivity of the authority's financial sustainability given alternative plausible scenario for the key drivers of costs, service demands and resources. It will require an analysis of future demand for key services and consideration of alternative options for matching demand to resources. Testing will focus on the key longer-term revenues and expenses and the key risks to which the authority will be exposed. Without such stress testing an authority cannot be regarded as financially sustainable and will be deemed to have failed that test.

81. The requirement to carry out a financial resilience assessment should be carefully distinguished from Statement of Standard Practice E5 by which authorities critically evaluate their financial management. Good financial management processes, validated by a critical evaluation, are important in promoting financial sustainability, but they do not guarantee that an authority has the resources to meet the demands placed on it.

Financial Management Standard F

The authority has carried out a credible and transparent Financial Resilience Assessment.

82. The starting point for this assessment will be an analysis of the latest audited financial statements. While external financial reporting (Section 7 of this Code) is in one sense the end of the financial management process it is also the starting point for the next cycle by providing a definite statement of the authority's financial position.

83. Importantly, the purpose of this financial resilience assessment is not to predict or forecast the future, but rather test and understand the authority's sustainability into an uncertain future. In this process optimism bias has to be avoided by encouraging critical challenge. The result will demonstrate that the authority understands its cost drivers and income sources and that the risks of existing delivery plans are clear and will inform the authority's strategic risk register.

Statement of Standard Practice F1

Financial resilience is tested against best and worst case scenarios which cover a wide range of financial demographic and social challenges.

84. One important way in which the objectivity of the financial resilience assessment can be demonstrated to be objective is by using an independent quantitative measure that allows the authority to measure and track the risks to which it is exposed. This is not achieved by ranking or comparison with other authorities but rather using an objective measure to identify financial risks.

> *Statement of Standard Practice F2*
>
> *The authority uses independent objective quantitate measures to assess the risks to its financial sustainability.*

85. The scope of the financial resilience assessment is likely to extend to an understanding of the risks associated with its most significant partners. This is necessary to ensure that essential public services are sustainable and to protect public body having to pay large compensation payments and from incurring other financial losses. When, as is common, a significant number of authorities are dependent on a single supplier then it may be valuable for those authorities to co-operate in this assessment in order to fully understand the risks.

86. Demonstrating the financial resilience of a local authority will require a focus on the contingency planning and development of exit strategies for key contracts. The risk management of these will form part of the good governance processes set out in Section 2 and the financial evaluation of the contractual arrangements themselves will form part of the business case process addressed in Section 5 below. Good practice would be demonstrated, for example, by the presence of partnering risks in a properly managed corporate risk register.

> *Statement of Standard Practice F3*
>
> *Decision making by the authority demonstrates a sound understanding of the risks associated with its strategic business partners.*

87. Having carried out the Finance Resilience Assessment, the authority will need to demonstrate how the risks identified have informed a Long Term Financial Strategy. A local authority needs an over-arching strategic vision of how it intends to deliver outputs and achieve outcomes for which it is responsible. This should include a statement that sets out both the vision and the underlying entity mission, together with the mix of interventions that the entity will adopt in delivering services to achieve the intended outcomes. In many cases a basis for this will already exist in a corporate plan.

88. A key part of the strategy should be a visioning exercise to understand the potential shape of services in the future. It will need to be sufficiently comprehensive to offer a convincing demonstration that the authority has identified a way of achieving financial sustainability. At the same time it needs to provide a relatively fixed point of reference which is subject to periodic review but subject to revision and fundamental change only when it is no longer fit for purpose.

Financial Management Standard G

The authority has a Long Term Financial Strategy for financial sustainability.

89. CIPFA is not at present being prescriptive about the time period of this Long Term Financial Strategy. Different authorities will face different levels of political and financial stability which may have become embedded in different management cultures. But CIPFA would promote ambition and stress the need for a financial strategy that matches the need for a strategic approach to service planning. The underlying demand for key costs drivers, especially those linked to the age profile of the community, can be foreseen at least in broad terms for a decade and more ahead.

90. Authorities with a high level of infrastructure investment and associated external borrowing should adopt a correspondingly long term approach. All authorities with PFI, service contracts and other similar contractual arrangements will need to demonstrate their ability to finance these arrangements over the whole period of the contracts. HRA business plans in England and Wales are already based on a 30 year time horizon.

91. The Long Term Financial Strategy will include proposals for which detailed implementation plans have yet to be developed. This presents a risk as some authorities have faced difficulties when ambitious transformation programmes based only on a promissory note of the potential for change have then failed to deliver. That said, ambition remains important so the solution is not to give up such ambition, but instead to find means (such as benchmarking) to carry out due diligence of such top-down programmes. These transformation programmes need still to be subject to sufficient 'due diligence' to enable the whole leadership team to be committed to the transformation programmes for which they are collectively responsible.

Managing the overall Balance Sheet

92. Balance sheet management in local authorities is about the better management of assets and liabilities to support service delivery capital strategy. A long term vision is needed for the configuration of service delivery and investment properties because timely asset disposals and/or investments will be dependent on complex interdependencies. A capital strategy, required by CIPFA's Prudential Code, is a fundamental component of good financial management, it should set out how the organisation is currently managing its assets and more importantly its future plans linked to available resources.

Financial Management Standard H

The authority has a capital strategy aligned to its long term financial strategy

93. The property assets of the authority raise specific issues, so the authority can be expected to have an Asset Management Plan that allows a full understanding of maintenance liabilities of the estate developed from a full programme of condition surveys. It should set out how priorities are addressed and be based on a 'whole life' approach to maintenance.

> Statement of Standard Practice H1
>
> The authority has an asset management plan that reviews the condition, sufficiency and suitability of assets in the light of business needs, and ambitions of the Medium - Long Term Financial Strategy
>
> The plan should evidence rigorous assessment of asset portfolio in relation to service delivery.

94. In addition to understanding its property assets, the authority needs to develop its long term financial strategy with an understanding of its other significant fixed assets and long term liabilities. A methodology for doing this is contained in *Balance Sheet Management in the Public Services: A Framework for Good Practice* (CIPFA, 2017).

> *Statement of Standard Practice H2*
>
> *The authority maintains processes to ensure that information about key assets and liabilities in its balance sheet is a sound and current platform for management action.*

The Prudential Code for Capital Finance in Local Authorities

95. The statutory requirements of the Prudential Code underpins elements of the long and medium term financial management considered in this section of the Financial Management Code. While the minimum requirement is for three year rolling capital and investment plans, paragraph E14 of the Prudential Code (2017 edition) stresses that a longer term approach is necessary to ensure that the capital strategy and asset management plans are sustainable.

> **Financial Management Standard I**
>
> **The authority complies with the CIPFA Prudential Code for Capital Finance in Local Authorities**

96. One of the requirements of the Prudential Code is the requirement for a capital strategy, as modified in England by *Statutory Guidance on Local Government Investments (3rd Edition)*. Through the Prudential Code mandating the *Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes (2017 Edition)* this will be accompanied by a treasury management strategy and investment plan.

97. CIPFA is not envisaging that the development of significant new reporting is required to demonstrate compliance with the CIPFA FM Code. The CIPFA Prudential Code

already requires authorities to demonstrate that the revenue consequences of proposed capital expenditure is affordable in both the short and long term. The FM Code adds to these minimum requirements the expectation that they will be applied on a longer term basis than has hitherto been the case.

Practical Medium Term Financial Planning

98. CIPFA does not anticipate that a Long Term Financial Strategy would provide sufficient detail to shape the annual budget setting process. Local authorities will need to translate their Long Term Financial Strategies into a Medium Term Financial Plan for budget setting. The Medium Term Financial Plan is the mechanism or framework by which the annual budget process relates directly to the long term strategy establishing the financial sustainability of the authority. Importantly, performance against the plan will enable recent success and/or failures in delivering financial objectives to be taken into account in the annual budget process. A symptom of financial stress is the emergence of unanticipated overspends in recent years of the Medium Term Financial Plan

99. The form of the Medium Term Financial Plan will be dependent upon the environment in which the authority exists, the challenges and opportunities it has identified and the level of infrastructure investment it makes. While the Long Term Strategy needs to be a stable point of reference, the Medium Term Financial Plan needs to be rolled forward annually to ensure that it reflects the latest detailed information.

100. The Medium Term Financial Plan should identify all the significant factors affecting the financial sustainability of the authority over the medium term. It includes specific quantitative and qualitative organisational targets and constraints. This plan balances the financial implications of objectives and policies against constraints in resources and provides the basis for decision making.

101. In contrast to the Long Term Financial Strategy, the Medium Term Financial Plan will be characterised by high quality plans to achieve its goals. A focus on the detail of execution is essential to turning policy goals into savings. For these reasons a ‘bottom up’ approach, starting point from a detailed understanding of current costs and business practices, is considered to be the preferred means of identifying savings in the medium to short term.

Financial Management Standard J

The authority has a rolling multi-year Medium Term Financial Plan

102. The Medium Term Financial Plan should enable the leadership team to have confidence in the concrete delivery of its long term strategy for its financial sustainability. Importantly, financial and operational plans must be demonstratively aligned to the strategy at all levels. Without clear service plans it is impossible to place the forecast within the context of currently agreed policies and their implications for future demand and resources.

Financial Management Standard K

The authority has sustainable service plans that are consistent with its Long Term Financial Strategy and Medium Term Financial Plan.

103. Integrated financial and service planning requires costings and other financial analysis to enable the leadership team to identify financial implications, assess and manage risk and promote the effective implementation of the financial strategy.

Statement of Standard Practice K1

The Medium Term Financial Plan should make reference to other organisational plans (e.g. workforce planning) and performance measures to demonstrate an alignment between service and financial planning.

104. CIPFA believes that the use of comparative data is essential to inform the development of credible service plans. Use of benchmarking data should be routine since every authority should have a firm understanding of how its costs and performance compare with comparable authorities. Councils should consider sharing information to identify basic facts, such as whether one provider is charging, without good reason, different authority' different prices for the same service. Local decisions reflecting different local demographics or decisions about service quality will create justified differences - but the implications of these local circumstances need to be made explicit.

Statement of Standard Practice K2

The authority has benchmarked the performance of its services against appropriate comparators.

105. A repeated failure to deliver financial and service plans may be a sign that an optimism bias is a feature of the calculations, such as making unrealistic assumptions about the quantity and pace of progress in achieving savings. A failure to plan and deliver savings in service provision to ensure the authority lives within its resources is a sign of financial stress. This builds up problems for future years. To ensure savings are delivered, each authority needs to develop in its Medium Term Financial Plan a single, consolidated, living document that tracks and evidences its saving plans – including what has been agreed and how much progress has been made. The savings plan should be formally provided to elected members and formally approved by Council.

Statement of Standard Practice K3

To inform the leadership team's decisions the authority has a single document tracking progress in the delivery of planned savings over the period of the Medium Term Financial Plan.

Reserves

106. Reserves are acknowledged in statute. Local authorities are directed to have regard to the level of reserves when considering its budget requirement. Consequently, reserves are a recognised and intrinsic part of financial planning and budget setting. The assessment of 'adequate' and 'necessary' levels of reserves is a matter for local authorities to determine. It is the responsibility of the Chief Finance Officer to advise the local authority on the appropriate level of reserves.

107. The assessment of the appropriate level of reserves, is a cornerstone of this Code. A well-managed authority will ensure that the reserves are not only adequate but are also necessary. There is a broad range within which authorities might reasonably operate depending on their particular circumstances, how this fits with the authority's financial strategy and how they will be used. CIPFA's latest guidance on these issues is to be found in *LAAP bulletin 99: Local Authority Reserves and Balances*.

108. In the absence of prescriptive legislation it has always been recognised that it should be a local decision to determine reserve levels. CIPFA's long held view has been that a generally applicable level of reserves is inappropriate, and that as a consequence it would stress that local authorities should have an approved strategy for its use of reserves. In setting clearer standards for financial management CPIFA intends to issue guidance to support the production of these strategies. In doing this care will be taken to distinguish contingencies from reserves and to recognise that authorities in different circumstances would have different risk appetite.

109. One sign of a systemic failure within the Medium Term Financial Plan is the unplanned use of usable reserves. The use of reserves is an acceptable budget financial strategy when it is done in recognition of the phased delivery of savings; but evidently it is not a sustainable alternative to a sustainable matching of financial plans to ongoing sustainable resources. To impose the necessary discipline the Medium Term Financial Plan should contain a clear statement on the planned and actual use of reserves.

Statement of Standard Practice K4

The authority publishes it plans for the use of reserves over the period of the Medium Term Financial Plan

The level of reserves at 31st March in any one year should not fall below the level previously agreed.

The authority should demonstrate adherence to the most recent guidance on reserves from CIPFA.

110. These plans for the use of reserves need to distinguish clearly between usable and unusable reserves and between the different uses to which usable reserves may be allocated. Reserves have a significant role in the effective financial management. As always some use of reserves to manage and cushion a clear and transparent savings programme over the medium term can be very sensible. However, the one-off use of reserves to avoid another cut in service level is unlikely to be good policy.

It does nothing to enhance financial sustainability and will make the following year even tougher in terms of the scale of cuts that have to be made.

Section 4: The Annual Budget

111. One of the principal objectives of this CIPFA FM Code is to end the practice by which the annual budget process has often become the focal point if not the limit of local authority financial planning. At the same time, the integrity of the annual budget preparation process needs to be protected at a time when the need to make difficult decisions may threaten its integrity.

112. The budget setting process of local authorities is closely regulated – from setting of budget, tax setting through to billing. The key principle is the council tax setting requirement:

- England, sections 31A, 42A of the Local Government Finance Act 1992 (as amended) and section 85 of the Greater London Authority Act 1999
- Wales, sections 32 and 43
- Scotland, 93 of the Local Government Finance Act 1992 and
- Rates (Northern Ireland) Order 1977 (as amended)

113. Local authorities need to ensure that they are familiar with these legislative requirements. In times of routine business compliance is straightforward, but in times of financial stress there may be pressures for delay or obfuscation in budget setting. In these circumstances it is likely that the Chief Finance Officer will need to work closely with the monitoring officer to ensure that the leadership team understand the statutory processes and timetable necessary to set a legal budget.

Financial Management Standard L

The authority complies with its statutory obligations in respect of the budget setting process.

114. The annual report setting out the proposed budget for the coming year is a key document for the authority, but it does not stand alone since its contents should flow consistently and clearly from the content of the long term financial strategy and medium term financial plan. It will also demonstrate compliance with CIPFA's Prudential Code (Financial Management Standard I) The best local budget plans are those owned and articulated by the whole leadership team and senior managers not simply the Chief Finance Officer .

Financial Management Standard M

The budget report includes an assessment of its consistency with the current medium term financial plan and long term financial strategy.

115. It is especially important that the budget report should include the document tracking relative success or failure in the achievement of a comparison with the previous year's performance which should form part of the Medium Term Financial Plan (section 3 of this Code). This is essential to inform the elected members and service directors in the leadership team to evaluate the realism of the coming year's plans. For example, if a service overspent or failed to meet its savings targets in the previous year, a degree of professional scepticism should be applied to whether a more challenging target could be achieved. The spirit of challenge should be objective but the reasons for any overspend need to be explained. Understanding the

causes of failure so they are not repeated will be an essential component of any challenge.

Statement of Standard Practice M1

The annual report proposing the budget includes an analysis of the success/failures in achieving the spending plans of the previous year and of departures from the planned use of reserves and balances.

116. This assessment of the past successes or failures in the achievement of budget reductions will inform the assessment by the Chief Finance Officer of the robustness of the estimates and the adequacy of the proposed financial reserves – in England, Wales and Northern Ireland this is a statutory responsibility of the Chief Finance Officer [2]. In fulfilling this important obligation the Chief Finance Officer may need to convey an unwelcome and challenging message as the principles of transparency must be uppermost. The council is required to take this statement into account when making its budget and taxation decisions. Experience has shown the Chief Finance Officers in authorities with financial resilience challenges are not always utilising this power to focus the mind of the organisation. This is therefore a subject on which CIPFA will be issuing guidance, including the use of objective measures of financial resilience.

Financial Management Standard N

The budget report includes a statement by the Chief Finance Officer on the robustness of the estimates and a statement of the adequacy of the proposed financial reserves.

117. The statement of reserves should list those earmarked reserves that are material for assessing the financial resilience of the authority. This statement should be a more detailed 'snap-shot' of the analysis used to inform the medium term financial plan considered earlier in Section 3. It should, for instance, set out transparently the purposes for which the reserves are held and show the estimated opening balances for the year, details of planned additions/withdrawals and the estimated closing balances.

118. This Code determines that a well-managed authority, with a prudent approach to budgeting should be able to operate with a level of general reserves appropriate for the risks (both internal and external) to which it is exposed. Compliance with the Code will give important reassurance that the authority's financial management is able to manage those risks. These should be maintained at a level appropriate for the profile of the organisation's cash flow and the prospect of having to meet unexpected events from within its own resources. Even where as part of their wider role auditors have to report on an authority's financial position, it is not their responsibility to prescribe the optimum or minimum level of reserves for individual authorities or authorities in general

[2] For E & W Local Government Act 2003 Section 25 NI chief finance officers' duty to report on the robustness of estimates and the
adequacy of reserves (under sections 4 and 6 of the Local Government and Finance Act (Northern Ireland) 2011

119. The successful execution of the annual budget will depend on both the good governance and internal controls already codified in Section 2 as well as financial monitoring addressed in Section 6 below.

Section 5 Stakeholder Engagement and Business Cases

120. Financial sustainability requires citizens to understand that resources are not limitless and that decisions have to be made about both the relative priority of different services and the balance between service provision and taxation levels. The leadership team collectively has an important role in reviewing priorities to enable resources to be redirected from areas of lesser priority; it is not possible to relying principally on pro rata cuts to generate the savings necessary for financial sustainability in an era of austerity.

121. The challenge must not only be to how services are delivered, but also to what is delivered. These decisions must be made with a clear understanding of the statutory requirements and of wider legal implications of any decisions. In making these often difficult decisions the special role of elected members and the democratic process must be respected; a feature of local government is that the leadership team contains both elected members with an executive role and their advisers.

Stakeholder Engagement

122. Stakeholder consultation at the earliest stage of preparing the long term financial strategy can help to set priorities and reduce the possibility of legal or political challenge late in the change process. Stakeholder consultation helps to encourage community involvement not just in the design of services but their ongoing delivery, promoting an enabling approach to public service delivery which, along with the active involvement of the third sector, may facilitate future reductions in service costs.

123. Stakeholder engagement is not just about public access to information but the active involvement of service users, stakeholders and partners in decisions about budgets, services, resource allocation and taxes. This is stressed in *Principle B of CIPFA/SOLACE Delivering Good Governance in Local Government: Framework (2016)* with which the CIPFA FM Code requires compliance. Local authorities require clear, trusted channels of communication to engage effectively with all groups of stakeholders. All stakeholders, including service users, must be able to feedback and influence the way the authority uses public funds and the services it provides. Communication and consultation methods should be balanced and fair. An authority’s processes should enable the interests of more vocal stakeholder groups to be balanced with other stakeholders' interests to ensure that no one group becomes too dominant.

124. Local democracy means that the residents are the primary stakeholders of local authorities. Consequently, local authorities will generally have a broader view of the issues affecting local communities and so will usually be in a better position to identify potential partners, bring commissioning and delivery bodies together, and then facilitate the development of shared aspirations and desired outcomes in response to those issues. But, in doing so, they will need to take account of the aims and objectives and associated sensitivities of potential partners.

125. This Code recognises that public service outcomes will not and cannot be achieved by any single body, sector or government. By focussing on outcomes at the start of the planning process, the involvement of stakeholders in the process encourages the identification of synergies with other public service providers to be identified as well as user input into how outcomes can best be achieved. The inextricable link between the outcome of achievements and allocation of resources means that authorities should extend the boundaries of cross- organisational engagement to include, for example, when appropriate:

- Health bodies;
- Charitable bodies
- Private sector partners and suppliers; and
- Other government bodies

126. The objective must be to avoid cost shunting, and rather to align local public services to maximise the synergies between them to reduce costs and improve services. CIPFA's publication *Aligning Local Public Services: The overview* sets out the context within which local bodies need to consider innovative ways in which to work in partnership to deliver local public services economically, effectively and efficiently

127. This engagement with local delivery partners should demonstrate consideration of alternative service delivery models, including joint service delivery and the practicality of delivery by external partners. In some authorities options of this type may be unpalatable to elected members of the leadership team and local politicians more generally. The Chief Finance Officer and other advisors on the leadership team therefore have an important responsibility to ensure that the costs and benefits of the elected members' preferred options are assessed against the other possibilities available. This may be done by the use of formal decision making techniques such as SWOT (strengths, weaknesses, opportunities, threats) and PESTLE (which focuses on external political, economic, social, technological, legal and environmental forces)

128. In addition to Council Tax and NNDR, local authorities have numerous income streams, from culture and sport to libraries, transport, waste management and parking. Decisions on such fees and charges often raise difficult political choices; but in reaching them elected members need clear information on the income options and likely impact. The necessity of systematically reviewing the affordability of non-statutory services will raise similar challenges. The authority will need to be responsive to its operating environment by seeking and responding to information on customer and stakeholder service and spending priorities that impact on its financial sustainability.

Financial Management Standard O

The authority has engaged with key stakeholders in developing its long term financial strategy, medium term financial plan and annual budget

Business Cases

129. Financial sustainability will be dependent upon difficult and often complex decisions being made. High-level vision statements are necessary, but they are not a substitute for sound financial assessments of policies and plans. The authority's

decisions must be informed by clear business cases informed by the application of appropriation option appraisal techniques.

Financial Management Standard P **The authority uses a documented option appraisal methodology to demonstrate the VFM of its decisions**

130. It is the responsibility of Chief Finance Officer's to ensure that all material decisions are supported by an option appraisal which is in its rigour and sophistication is appropriate for the decision being made. It is likely that the authority's documented option appraisal methodology will include a simple approach for decisions of low value and/or low risk.

Statements of Standard Practice P1 *Option appraisal complies with IFAC/PAIB Project and Investment Appraisal for Sustainable Value Creation: Principles in Project and Investment Appraisal (Annex C to this Code)*

131. Any division and separation between financial and management accounting in developing business cases is untenable since required accounting treatments will determine the implications for the General Fund balance. To wait until the accounts closure process to determine the correct accounting treatment may be too late. The financial implications of material decisions and alternative service delivery models will often be dependent on the correct application of financial reporting standards. This will especially be the case for innovative partnership arrangements or new forms of capital investment. The accounting implications of policy decisions should be addressed and clearly demonstrated as part of the decision making process.

Statement of Standard Practice P2 *The accounting treatment of material decisions is considered and demonstrated as part of the formal option appraisal process.*

132. Once the financial reporting standards have been correctly applied to each option, the application of an option appraisal methodology and the presentation of the results in an informative way to the leadership team is reliant of proper costing techniques. Hitherto management accounting had not been governed by a framework of international standards familiar to financial accountants, but this is changing with initiatives such as the IFAC/PAIB Project and Investment Appraisal for Sustainable Value Creation: Principles in Project and Investment Appraisal. CIPFA's Service Reporting Code of Practice (SeRCOP), originally introduced to promote consistent financial reporting by local government, and now also provides the management accounting standards for the production of statistical and benchmarking data for local authorities.

Financial Management Standard Q

The authority applies the principles contained in the CIPFA Service Reporting Code of Practice and utilises appropriate costing techniques in the development of business cases

133. CIPFA's Service Reporting Code of Practice (SeRCOP) includes a formal definition of total cost which must be used, for instance, in statistical returns to central government or when the full cost of a service needs to be recovered. However the SeRCOP stresses that total cost may not always be appropriate. Costing for decision-making purposes will often require the use of different techniques; it will also require that all relevant costs, and only relevant costs, are taken into account, whether they form part of total cost or not. For example, there are strong arguments for reflecting the costs of early retirement in management accounts so that service managers can see the cost as well as the benefit of such decisions, and as a way of ensuring management discipline. Such costs are not within the SeRCOP total cost of individual services for consistency reasons, and so parallel accounting systems may be required, using total cost for external reporting, charging and comparisons and other accounts for internal management purposes.

134. Authorities will also need to decide whether the revenue cost of capital arising from, for example, interest charges element (to reflect the full cost of using non-current assets in the provision of a service) should be included in any costing for decision-making or charging purposes.

Section 6: Performance Monitoring

135. To remain financially sustainable an authority must have timely information on its financial and operational performance so that policy objectives are delivered within budget. Early information about emerging risks to its financial sustainability will allow it to make a carefully considered and therefore effective response.

> **Financial Management Standard R**
>
> **The leadership team takes action using reports enabling it to identify and correct emerging risks to its budget strategy and financial sustainability.**

136. Significant unplanned overspends and/or carrying forward undelivered saving into the following year are a sign that an authority is not translating its policy decisions into actions. It also creates the conditions for further financial pressures and possibly service reductions in subsequent years. But the warning signs could be in other non-financial performance measures, such as backlogs and other indications that current resources are not matching the expectations of service users. These trends should inform the decisions taken on the medium and long term financial planning addressed by Section 3 of this Code.

137. The first line of defence against budgetary failure is the quality of information available to managers. Front line service managers and budget holders will want to ensure that financial and service performance are aligned with budget plans. An authority needs an effective finance systems that provides all decision makers with one version of the truth.

> *Statement of Standard Practice R1*
>
> *Timely financial and performance information is available to managers via the appropriate systems.*
>
> *Financial and performance management systems are engineered to provide relevant data at a sufficiently accurate level.*
>
> *When appropriate, budgets are profiled to support effective budgetary control through the financial year.*
>
> *The organisation ensures that information is appropriately tailored and streamlined to avoid the risk of 'data overload'.*

138. At its most basic, financial monitoring is necessary to allow control over spending and service delivery. For this purpose financial and other management information needs to be accurate and timely and embedded in a system of internal control that focusses on controls, probity, compliance and accountability. But financial management information is only valuable if it results in action. For this purpose the real time financial and performance information needs to be periodically collated for management review and action. Most importantly, the details of these performance monitoring arrangements must ensure that personal responsibility for each budget is

established and recognise that routine longstanding but still best practices are followed.

Statement of Standard Practice R2 *All Financial monitoring reports include:* *- The name of the budget holder responsible for the information presented* *- Accruals based financial information* *- Include the approved budget against which monitoring is taking place.* *- A forecast for the remainder of the budget period,* *- Service performance information and* *- is shown, for instance by reconciliations, to be consistent with the aggregate position for the authority.*

139. Responsibility for the aggregate of a local authority's budgets is the responsibility of the leadership team. The information presented needs to be sufficient for the team to determine whether there is any necessity to revisit the medium term financial plan and even long term financial strategy. The causes of budget over or under spends may not be immediately obvious, so the presentation of this information needs to be accompanied by an analysis of the causes. These could be changes or unexpected developments in the external environment or in the internal operations of the authority.

Statement of Standard Practice R3 *Financial monitoring reports for high risk budgets are:* *- Scrutinised by the leadership team of the organisation on (as a minimum) monthly basis.* *- Financial monitoring reports for steady state/low risk budgets are:* *-Received by budget holders on a monthly basis* *-Received (in aggregate) by the leadership team on a regular basis (in aggregate) by the leadership team.*

140. Financial monitoring should act as catalyst for timely intervention in advance of the annual budget setting process. Responsibility for addressing budgetary failures must in the first instance rest with budget holders. There still needs, however, to be a process for amending service budgets when they have been subject to fundamental changes to the operational environment. It is important that steps are taken to maintain budgetary discipline in such circumstances as otherwise a loss of control would undermine the financial sustainability of that service or even the authority. Except in the most extreme circumstances, it is likely that the overspending of some budgets will be accompanied by the underspending of others. An authority needs to be clear as to which emerging underspends may be retained by the budget holder and which should be corporately pooled in support of the financial sustainability of

the authority. Wider assessment will determine whether any underspend indicates a failure of performance or failure to deliver services.

141. The leadership team needs to have clear criteria which determine when such budget flexibility is appropriate; budgetary control is undermined if frequent amendments become the norm. These exceptional in-year changes should usefully be distinguished from the general revision or recalibration of in-year budgets which typically takes place when the detailed budget for the forthcoming year is prepared.

Statement of Standard Practice R4

The authority has arrangements which allow annual service budgets to be recalibrated in response to unforeseen developments.

142. The overall financial performance of an authority will be determined not only by service expenditure controlled by operational managers, but also by "below the line" non-service budgets for which expenditure is controlled corporately. These will vary according to the particular management arrangements of the authority. It is therefore important that the leadership team report receives a regular comprehensive update that sets the regular financial monitoring information in its wider context.

Statement of Standard Practice R5

At the financial monitoring period end the leadership team receives a set of financial statements with forecast outturn for the year ahead

143. In addition the financial sustainability of the authority may be affected by the performance of partners and subsidiaries in which it has a financial interest. Financial and risk management needs to take place at the level of the group entity and not just of the level of the local authority parent. Recent experience with Carillion has shown that even the largest companies providing outsourcing and public service are not necessarily as financially sustainable as their size and prominence in the market would suggest. Financial pressures have also created a new level of interest around commercial arrangements. In some cases these have become a method to balance the books or promise future financial sustainability, which brings both new and often large risks.

Statement of Standard Practice R6

There are appropriate arrangements in place for reporting and managing the financial performance of each of the organisation's delivery partnerships and collaborative arrangements.

144. The project management and cost control of capital projects is a specialist skills which are of critical importance if local authorities are to deliver the financial savings and improved service depended on the timely completion of complex schemes.

Statement of Standard Practice R7

There are appropriate arrangements in place for the project management and cost control of capital projects.

145. Local authorities do not customarily monitor the 'in year' performance of their balance sheet, beyond possibly tracking the use of balances. This contrasts with the private sector, in which the production a monthly balance sheets is common practice. The regularly production of a balance sheet brings with it costs that, historically have been judged to be too high by authorities. Increasing the use of capital resources and complex financial transactions means that more attention should now be given to the balance sheet to gain an understanding of significant assets and long term liabilities. A methodology for doing this is contained in *Balance Sheet Management in the Public Services: A Framework for Good Practice* (CIPFA, 2017).

146. It is a requirement of this Code that authorities should more closely monitor the material elements of their balance sheet that may give indications of a departure from financial plans. This is especially important for local authorities with significant commercial asset portfolios. The recording of assets and liabilities, and the ability to report on these, can also be a statutory responsibility for authorities.[3]

Financial Management Standard S

The leadership team monitors the elements of its balance sheet which pose a significant risk to its financial sustainability.

Statements of Standard Practice S1

Unplanned and planned use of reserves are reported [quarterly] to the management team of the organisation and to Council.

Statement of Standard Practice S2

Management accounts include an appropriate level of balance sheet information to meet business needs and evidence of monitoring of material items

147. Local authorities should, for example be interested in their unusable reserves as these include liabilities that the council tax setting and other statutory provisions have allowed local authorities to defer to be charged against taxation and reserves in future years. Contingencies and commitments are monitored to identify any items where a balance sheet provision may have crystallised. Key drivers of provisions (eg asset decommissioning decisions, legal claims, reorganisation activities) should be monitored to identify whether an actual or constructive obligation has arisen. Finally, cash flow is managed through application of *Treasury Management in the Public*

[3] As specified by: see SI 2015/234 - Local Government, England And Wales
The Accounts and Audit Regulations 2015 Section 4; SSI 2014/200 The Local Authority Accounts (Scotland) Regulations 2014 Section 6 – especially sub-section 2 (b); WSI 2014/3362 (W337) The Accounts and Audit (Wales) Regulations 2014 section 6 – especially sub-section 2 (b); and NISR 2015/106 The Local Government (Accounts and Audit) Regulations (Northern Ireland) 2015 Section 5.

Services: Code of Practice and Cross-Sectoral Guidance Notes (CIPFA 2017). Compliance with the Treasury Management is a requirement of satisfying the Prudential Code (Financial Management Standard I.)

Section 7: External Financial Reporting

148. Taxpayers and citizens have a legitimate stake in understanding how public money has been used and managed so they have typically been seen as the audience of external financial reporting. But the customary distinction between internal financial management and external financial reporting should be treated with extreme caution. In providing the definitive audited statement of the authority's financial position and financial performance, the statutory accounts provide a secure foundation for financial management. This supports accountability and thus good financial management by allowing the leadership team and other stakeholders to:

- discover how much is spent in a year on services and whether this has increased or decreased from previous years
- consider the indebtedness of an organisation and how that might impact on future taxpayers
- recognise the value and therefore usefulness of the assets that the organisations hold
- assess what the future commitments and liabilities are, for example, for pensions or leases, and again how these are likely to impact on future generations and taxpayers.

149. The external financial reporting process in local authorities is substantially regulated by statutory provisions both in primary and secondary legislation. Local authorities are required to produce their statutory statements of accounts (annual accounts in Scotland) on an annual basis in accordance with:

- the Accounts and Audit Regulations 2015 for English Authorities
- the Local Government (Accounts and Audit) Regulations Northern Ireland 2015
- the Local Authority Accounts (Scotland) Regulations 2014
- the Accounts and Audit (Wales) Regulations 2014.

150. These regulations all require that local authorities present a 'true and fair' view of the financial performance and financial position of the authority. Separate statutory provisions also require that local authorities follow proper accounting practices which include regulations but also importantly include the Code of Practice on Local Authority Accounting in the United Kingdom which is issued annually.

151. CIPFA's statement on the role of the Chief Finance Officer Local Government sets out the Chief Finance Officer responsibilities for producing the accounts and financial records for those accounts. The CIPFA Statement requires that the annual accounts are published on timely basis to communicate the authority's activities and achievements, its financial position and performance and requires certification of the accounts by the Chief Finance Officer. The confirmation that the accounts present a 'true and fair' view is one of the fundamental roles of the statutory Chief Finance Officer.

Financial Management Standard T

The Chief Finance Officer has personal responsibility for ensuring that the statutory accounts provided to the local authority comply with the *Code of Practice on Local Authority Accounting in the United Kingdom.*

152. The statutory and professional frameworks for the production and publication of the accounts underpin their importance and demonstrate that they have a key part to play in accountability to taxpayers and other stakeholders showing how public money is used. The importance of the budget and budget monitoring for local authorities is paramount and is discussed in detail in other parts of this Code but without the audited statement of accounts to confirm the outturn for previous year there can be no assurances about the baseline on which the current budget is founded. Financial reporting therefore should not take place in a vacuum. It must provide the accountability link between planned performance and spending and the outcomes – financial and more – that are achieved. The authority, its management and the Chief Finance Officer, must provide the user with the links between the consumption of resources and the value that has been created.

153. It is key therefore that the budgetary process is brought together with the veracity of the financial reporting process to ensure that the council, its leadership and governance understand how effectively its resources have been utilised during the year including a process which explains how material variances from initial and revised budgets have arisen and been managed. The success of these arrangements will be demonstrated by the ability of the leadership team to make decisions from them.

Financial Management Standard U

The presentation of the final outturn figures and variations from budget allow the leadership team to make strategic financial decisions.

154. The presentation of the annual accounts both closes the financial management cycle and initiates the start of the next financial cycle with the rolling forward and review of the medium term financial plan and in some circumstances a reappraisal of the credibility of the long term financial strategy and the financial resilience of the authority (Section 3 above).

Financial Resilience and Financial Reporting

155. The statutory accounts will provide important information on the financial sustainability of the authority though it should be underlined that it is not the only source of this information. Regulations across the UK determine what councils can charge to the General Fund and hence against income and expenditure in a particular year. The most significant of these statutory accounting requirements under the regulations for most local authorities are the IAS 19 (Employee Benefits as adopted by the Code) pension reserve position and/ or the statutory accounting entries for capital finance with the capital adjustment account. While items such as pensions liabilities and depreciation may not immediately affect the authority's usable reserves, an understanding of the extent of these unfunded liabilities is critical to reaching a conclusion on intergenerational equity and exposing the burden being built up for future taxpayers.

156. The local authority balance sheet is based on IFRS (as adopted by the Code) and includes liabilities that local authorities may not fund using taxpayer resources until a future date. When an authority has a negative net worth, this indicates that future taxpayers (whether through Council Tax or indirectly through government grants) will be funding some of the cost of providing services which have been delivered in

the past.

157. It is likely that there are a number of authorities who are already in a negative net worth position. This doesn't mean they are not a going concern. Local authorities are required to operate within the financial reporting framework set out in the Local Government. As a consequence, while authorities must budget for a positive General Fund Balance, they are not required to maintain a positive net worth. It will be important that this position is presented effectively to the readership of the financial statements in accordance with the requirements of the Accounting Code.

158. In demonstrating that they are a going concern basis, local authorities need to show that they are able to meet their liabilities according to when that is legally required by the regulations, not immediately when these liabilities are recognised in accordance with the accounting requirements in the IFRS-based Code i.e. those accounting requirements in the Code that are based on IFRS only (the Code also includes the statutory accounting requirements). This approach should ensure liabilities such as the pension's liability are met in the long run. The future funding of these liabilities will be met mainly by a combination of council tax (which authorities have a legal power to raise) business rates, and local government finance settlements. It is expected that future cash flows, aligned with authorities' budget processes, will provide sufficient resources to finance future liabilities, and hence a going concern basis is appropriate.

159. Notwithstanding these general comments an authority will need to consider whether the effect of the authority's negative net worth results in any going concern issues for any part of the authority, this is normally unlikely to be the case if the negative net worth position is as a result of the timings of the statutory requirements as outlined above.

160. One of the objectives of the financial statements is to present the economic activity of the council i.e. its financial position and financial performance so that it is useful to a wide range of users for assessing the stewardship of an authority's management and for making economic decisions. Financial reporting standards as adopted by the Code require expenditure to be recorded irrespective of whether it is funded or unfunded. So where expenditure has been incurred the Code requires that it is properly recognised in the Comprehensive Income and Expenditure Statement. Where expenditure exceeds income a deficit will be recognised in accordance with the presentation requirements of that Statement.

161. Where the deficit position and other adjustments to General Fund balances mean that the cumulative position is such that the General Fund is in deficit this will be recognised in the Balance Sheet – this is likely also to be at the point at which the Chief Finance Officer should be taking appropriate statutory action as discussed in earlier chapters. Explanatory notes and appropriate description will be required if this has a material impact on the presentation of a local authority's financial performance (the Comprehensive Income and Expenditure Statement) and its financial position (the Balance Sheet).

Stakeholder Engagement and Financial Reporting

162. Section 5 of this Code recognises the importance of effective stakeholder engagement. Traditionally, any external engagement in financial reporting arises directly and solely from the statutory financial reporting requirements. Increasingly complex financial information can be difficult to communicate effectively to a lay audience. Nevertheless, the need to report externally (irrespective of complexity) has increased in recent years and the demand for local authority financial information is not restricted to the period associated with the financial statements.

163. This Code requires Chief Financial Officers to actively engage with stakeholders and to determine a local strategy to produce regular external financial information in addition to annual financial statements. Financial information can be provided in a range of formats, which includes, but is not restricted to:

- Simplified financial statements;
- Extracted key points of information from time to time such as financial instruments, assets, investment properties for specified audiences;
- Simplified or summarised information which reports periodic progress against budget (as reported to elected members);
- The indexed position of the local authority as included within CIPFA's index/dashboard
- The level of local taxation and how it relates to local service delivery.

	Section 1 The Responsibilities of the Chief Finance Officer
A	**The leadership team demonstrates that the services provided by the authority provide value for money.**
B	**The authority complies with the CIPFA Statement on the Role of the Chief Finance Officer in Local Government**
B1	The Chief Finance Officer in a public service organisation is a key member of the leadership team, helping it to develop and implement strategy and to resource and deliver the organisation's strategic objectives sustainably and in the public interest. [From CIPFA: The Role of the Chief Financial Officer in Local Government (2016) p 7]
B2	The Chief Finance Officer must be actively involved in, and able to bring influence to bear on, all material business decisions to ensure immediate and longer term implications, opportunities and risks are fully considered, and alignment with the organisation's financial strategy. [From CIPFA: The Role of the Chief Financial Officer in Local Government (2016) p 7] Organisations which are required to explain (rather than comply) should set out clearly how the associated risks will be managed and demonstrate notification of the risks to the political leadership.
B3	The Chief Finance Officer must lead the promotion and delivery by the whole organisation of good financial management so that public money is safeguarded at all times and used appropriately, economically, efficiently and effectively. [From CIPFA: The Role of the Chief Financial Officer in Local Government (2016) p 7] The Chief Finance Officer should regularly review the skillsets of elected members and all officers with budget/financial management responsibility and ensure appropriate support is provided.
B4	The Chief Finance Officer must lead and direct a finance function that is resourced to be fit for purpose [From CIPFA: The Role of the Chief Financial Officer in Local Government (2016) p 7] The Chief Finance Officer should regularly review the skillsets of all finance staff with senior budget/financial management responsibility and ensure ongoing appropriate support is provided. The ratio of qualified staff as a proportion of total finance staff ensures that the finance function has the necessary financial competence.
B5	The Chief Finance Officer must be professionally qualified and suitably experienced. [From CIPFA: The Role of the Chief Financial Officer in Local Government (2016) p 7] The Chief Finance Officer must be able to demonstrate adherence to professional CPD requirements on an annual basis

B6	The Chief Finance Officer should promote the highest standards of ethical behaviour in the conduct of financial management. Professionally qualified staff should evidence ongoing benchmarking against the principles of objectivity, integrity professional behaviour, professional competence, dues care and confidentiality.
B7	To enable financially informed decision making: The Chief Finance Officer should be able to provide the leadership team with sound advice on the key principles of local government finance; and The Chief Finance Officer should be able to demonstrate a sound system which ensures the authority has access to high standards of technical financial advice.
B8	The chief finance officer should report explicitly on the affordability and risk associated with the capital strategy and where appropriate have access to specialised advice to enable them to reach their conclusions. [The Prudential Code for Capital Finance in Local Authorities 2017 Edition Page 13]
B9	The chief finance officer must establish the reporting and monitoring processes, and integrate the treasury management indicators into the overall financial planning process [CIPFA Treasury Management in The Public Services, Guidance Notes For Local Authorities Including Police Forces And Fire And Rescue Authorities (2018 Edition) p9]
B10	The Chief Finance Officer of Local Government Pension Scheme (LGPS) administering authorities satisfies the requirements of the CIPFA Code of Practice on Public Sector Pensions Finance Knowledge and Skills (2013 edition)
	Section 2 Governance and Management Style
C	**The leadership team demonstrates in its actions and behaviours responsibility for governance and internal control.**
D	**The authority applies the CIPFA/SOLACE Delivering Good Governance in Local Government: Framework (2016)**
D1	The authority maintains an effective audit committee
D2	The audit committee receives and monitors the implementation of internal and external audit recommendations. When threats to the financial sustainability of the authority are identified by auditors the audit committee should ensure that the recommendations are communicated to the leadership team and that the committee are informed of the effectiveness of the leadership team’s response.
D3	The authority has a PSIAS conformant internal audit function
E	**The Financial Management Style of the authority supports financial sustainability**

E1	The organisation has an effective framework of financial accountability that is clearly understood and applied throughout, from the political leaders, elected members to directors, finance officers and front line service managers. [Adapted from CIPFA FM Model]
E2	Finance teams and the organisation they support are actively committed to continuous improvement focused on efficient and effective delivery and organisational performance. The organisation has an effective framework of financial accountability that is clearly understood and applied throughout, from the political leaders, elected members to directors, finance officers and front line service managers. [Adapted from CIPFA FM Model]
E3	Enabling transformation: the finance team have input into strategic and operational plans taking into account proactive risk management, clear strategic directions and focus-based outcomes
E4	Managers understand they are responsible for delivering services cost effectively and are held accountable for doing so. Financial literacy is diffused throughout the organisation so that decision takers understand and manage the financial implications of their decisions.
E5	The financial management of the authority has been critically evaluated
	Section 3: Long to Medium Term Financial Management
F	**The authority has carried out a credible and transparent Financial Resilience Assessment.**
F1	Financial residence is tested against best and worst case scenarios which cover a wide range of financial demographic and social challenges.
F2	The authority uses independent objective quantitate measures to assess the risks to its financial sustainability.
F3	Decision making by the authority demonstrates a sound understanding of the risks associated with its strategic business partners.
G	**The authority has a Long Term Financial Strategy for financial sustainability.**
H	**The authority has a capital strategy aligned to its long term financial strategy**
H1	The authority has an asset management plan that reviews the condition, sufficiency and suitability of assets in the light of business needs, and ambitions of the Medium - Long Term Financial Strategy The plan should evidence rigorous assessment of asset portfolio in relation to service delivery.

H2	The authority maintains processes to ensure that information about key assets and liabilities in its balance sheet is a sound and current platform for management action.
I	**The authority complies with the CIPFA Prudential Code**
J	**The authority has a rolling multi-year Medium Term Financial Plan**
K	**The authority has sustainable service plans that are consistent with its long term financial strategy and the medium term financial plan.**
K1	The Medium Term Financial Plan should make reference to other organisational plans (e.g. workforce planning) and performance measures to demonstrate an alignment between service and financial planning.
K2	The authority has benchmarked the performance of its services against appropriate comparators.
K3	To inform the Leadership Team’s decisions the authority has a single document tracking progress in the delivery of planned savings over the period of the Medium Term Financial Plan.
K4	The authority publishes it plans for the use of reserves over the over the period of the Medium Term Financial Plan The level of reserves at 31st March in any one year should not be fall below the level previously agreed. The authority should demonstrate adherence to the most recent guidance on reserves from CIPFA’s Local Authority Accounting Panel
	Section 4: The Annual Budget
L	**The authority complies with its statutory obligations in respect of the budget setting process**
M	**The budget report includes an assessment of its consistency with the current medium term financial plan and long term financial strategy.**
M1	The annual report proposing the budget includes an analysis of the success/failures in achieving the spending plans of the previous year and of departures from the planned use of reserves and balances.
N	**The budget report includes a statement by the Chief Finance Officer on the robustness of the estimates and a statement of the adequacy of the proposed financial reserves.**
	Section 5: Stakeholder Engagement and Businesses Cases
O	**The authority has engaged with key stakeholders in developing its long term financial strategy, medium term financial plan and annual budget.**
P	**The authority uses a documented option appraisal methodology to demonstrate the VFM of its decisions**

<table>
<tr><td>P1</td><td>Option appraisal IFAC/PAIB Project and Investment Appraisal for Sustainable Value Creation: Principles in Project and Investment Appraisal (Annex C to CIPFA FM Code)</td></tr>
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Accruals based financial information
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A forecast for the remainder of the budget period,
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R6	There are appropriate arrangements in place for reporting and managing the financial performance of each of the organisation's delivery partnerships and collaborative arrangements.
R7	There are appropriate arrangements in place for the project management and cost control of capital projects.
S	**The authority monitors the elements of its balance sheet which pose a significant risk to its financial stability**
S1	Unplanned and planned use of reserves are reported [quarterly] to the management team of the organisation and to Council.
S2	Management accounts include either a full balance sheet or an appropriate level of balance sheet information to meet business needs and evidence of monitoring of material items
	Section 7 External Financial Reporting
T	**The Chief Finance Officer has personal responsibility for ensuring that the statutory accounts provided to the local authority comply with the Code of Practice on Local Authority Accounting in the United Kingdom..**
U	**The presentation of the final outturn figures and variations from budget allow the leadership team to make strategic financial decisions.**

IFAC/CIPFA Guidance on Implementing the Principles For Good Governance in the Public Sector (extract)

PRINCIPLES FOR GOOD GOVERNANCE IN THE PUBLIC SECTOR

Governance comprises the arrangements put in place to ensure that the intended outcomes for stakeholders are defined and achieved.

The fundamental function of good governance in the public sector is to ensure that entities achieve their intended outcomes while acting in the public interest at all times.

Acting in the public interest requires:

A. Behaving with integrity, demonstrating strong commitment to ethical values, and respecting the rule of law

B. Ensuring openness and comprehensive stakeholder engagement

In addition to the overarching requirements for acting in the public interest in principles A and B, achieving good governance in the public sector also requires effective arrangements for:

C. Defining outcomes in terms of sustainable economic, social, and environmental benefits

D. Determining the interventions necessary to optimize the achievement of the intended outcomes

E. Developing the entity's capacity, including the capability of its leadership and the individuals within it

F. Managing risks and performance through robust internal control and strong public financial management

G. Implementing good practices in transparency, reporting, and audit to deliver effective accountability.

CIPFA/ SOLACE Delivering Good Governance in Local Government: Framework \ 2016 Edition Core principles of good governance

Acting in the public interest requires a commitment to and effective arrangements for:

A. Behaving with integrity, demonstrating strong commitment to ethical values, and respecting the rule of law
B. Ensuring openness and comprehensive stakeholder engagement
C. Defining outcomes in terms of sustainable economic, social, and environmental benefits
D. Determining the interventions necessary to optimise the achievement of the intended outcomes
E. Developing the entity’s capacity, including the capability of its leadership and the individuals within it
F. Managing risks and performance through robust internal control and strong public financial management
G. Implementing good practices in transparency, reporting, and audit to deliver
H. effective accountability

IFAC/PAIB Project and Investment Appraisal for Sustainable Value Creation (Extract from https://www.ifac.org/publications-resources/project-and-investment-appraisal-sustainable-value-creation-1)

PRINCIPLES IN PROJECT AND INVESTMENT APPRAISAL

The key principles underlying widely accepted good practice are:

A. When appraising multi-period investments, where expected benefits and costs and related cash inflows and outflows arise over time, the time value of money should be taken into account in the respective period.

B. The time value of money should be represented by the opportunity cost of capital.

C. The discount rate used to calculate the NPV in a DCF analysis should properly reflect the systematic risk of cash flows attributable to the project being appraised, and not the systematic risk of the organization undertaking the project.

D. A good decision relies on an understanding of the business and should be considered and interpreted in relation to an organization's strategy and its economic, social, environmental, and competitive position as well as market dynamics.

E. Project cash flows should be estimated incrementally, so that a DCF analysis should only consider expected cash flows that could change if the proposed investment is implemented. The value of an investment depends on all the additional and relevant changes to potential cash inflows and outflows that follow from accepting an investment.

All assumptions used in undertaking DCF analysis, and in evaluating proposed investment projects, should be supported by reasoned judgment, particularly where factors are difficult to predict and estimate. Using techniques such as sensitivity analysis to identify key variables and risks helps to reflect worst, most likely, and best case scenarios, and, therefore, can support a reasoned judgment.

G. A post-completion review or audit of an investment decision should include an assessment of the decision-making process and the results, benefits, and outcomes of the decision.

Capital and revenue reports need to be closely linked so there is an understanding of how each capital scheme is financed, and in particular which require revenue contributions.

Borrowing costs need to be spelt out. Low interest rates are not in themselves a compelling reason to borrow. Capital budgets should be clear about how individual schemes are financed and which ones add pressure to revenue.

Accounting Standards

Rules set by the International Accounting Standards Boards that set out how transactions are to be shown in an organisation's accounts.

Annual Statement of Accounts

An annual statement setting out the income and expenditure of the council along with its assets and liabilities.

Audit Committee

A special committee of the council that reviews the financial management and accounts of the council.

Balance Sheet

A statement showing the assets and liabilities of the council.

Capital Budget

The money a council spends on investing in new buildings, infrastructure and expensive pieces of equipment.

Capital Financing Charges

The amount a council has to pay to support its borrowing to pay for the purchase of major assets.

Capital Receipt

The money a council receives for selling assets that can only be used to repay debt or for new capital expenditure.

Chief Financial Officer

The most senior finance person in a council responsible for ensuring the proper financial management of the council.

Code of Practice on Local Authority Accounting in the United Kingdom

A code produced by CIPFA/LASAAC that sets out how councils should show transactions in their accounts and the format of the accounts.

Earmarked Reserve

Money set aside for future use on a specific area of expenditure.

External Audit

An external review of the council's accounts and systems.

Governance

The framework by which a council can gain assurance that it is setting and achieving its objectives and ensuring value for money in the proper way.

Housing Revenue Account (HRA)

An account used to record the income and expenditure related to council housing.

Internal Audit

An internal review of the organisation's systems to give assurance that they are appropriate and being complied with.

Leadership Team

Executive committees, elected mayors, portfolio holders with delegated powers and other key committees of the authority. In the police service this leadership is provided by Police and Crime Commissioners and Chief Constables.

Non-domestic Rates

A tax paid by local businesses to their council.

Provision

Money set aside against a specific future liability.

Prudential Code

A code produced by CIPFA that councils are required to follow when deciding upon their programme for capital expenditure.

Revenue Budget

The amount that a council spends on its day-to-day running of services through the financial year.

Ringfencing

A term for the earmarking of money (eg a grant or fund) for one particular purpose, so as to restrict its use to that purpose.

Treasury Management

The management of the cash balances and borrowing needs arising from the council's cash flows.

Treasury Management Code

A code produced by CIPFA that councils are required to follow in managing their treasury management activity.

Treasury Management Strategy

An annual document approved by full council that sets out how a council will manage its cash and borrowings.

[List of codes, guidance and publications referred to or relevant]

[Incomplete draft list for illustrative purposes.]

Audit Commission Strategic Financial Management in Councils: Delivering Services with a Reduced Income (2010)

CIPFA, Code of Practice on Local Authority Accounting in the United Kingdom 2018/19

CIPFA The Prudential Code for Capital Finance in Local Authorities (2017 Edition)

CIPFA Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes (2017 Edition)

CIPFA Code of Practice on Public Sector Pensions Finance Knowledge and Skills (2013 Edition)

CIPFA Pensions Finance Knowledge and Skills framework: Technical Guidance for Pensions Practitioners in the Public Sector (2010)

CIPFA's Position Statement: Audit Committees in Local Authorities and Police 2018

CIPFA/IFAC International Framework: Good Governance in the Public Sector

CIPFA The Role of the Chief Financial Officer in Local Government

CIPFA/SOLACE Delivering Good Governance in Local Government: Framework (2016 Edition)

CIPFA/SOLACE Delivering Good Governance in Local Government: Framework Review of annual governance statements 2016/17

CIPFA (Insight) Looking Forward: Medium-term financial strategies in the UK public sector

CIPFA (Insight) Building Financial Resilience Managing Financial Stress in Local Authorities

CIPFA (Insight) Accountability, performance and transformation Learning from the CIPFA FM Model

CIPFA (Insight) Balancing Local Authority Budget

CIPFA Financial reporting in the public sector An Introductory Guide to in the United Kingdom

CIPFA Audit Committees: Practical Guidance for Local Authorities and Police (2018 Edition)

CIPFA Delivering Excellent Public Finance: CIPFA's Whole System Approach to Public Financial Management Volumes 1 and 2

IASAB Public Sector Internal Audit Standards

National Audit Office, Financial Management Maturity Model