



Strategic Public Finance Exam (March 2024)

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Short-termism leaves public services in 'doom loop'

Most public services will remain worse in four years' time than they were just before Covid-19 – and most of them were already worse than they were in 2010 – CIPFA and the Institute for Government's annual stocktake has found.

Under-investment in capital has left public sector workers dealing with crumbling, cramped buildings with outdated equipment, leading to poor productivity and a workforce crisis, according to this year's Performance Tracker.

The report looked at general practice, hospitals, adult social care, children's social care, neighbourhood services, schools, police, criminal courts and prisons – and found government spending decisions will probably mean all services apart from children's care will be worse in 2027-28 than they were in 2019-20. It warned the spending plans have left services in a "doom loop" of crisis, with burnt-out staff and short-term decisions.

"After a year of significant political and economic turmoil, the public sector is crying out for a shift to longer-term planning, rather than the short-term thinking that has been a central feature of recent policy-making," said CIPFA chief executive. He hopes the report will serve "as a reminder of just how damaging the past few years have been to the sector, and that it will act as a roadmap to building better and more resilient services for all."

The report suggested a new sufficient multi-year budget for each public service, long-term capital programme, stable government policy agenda and a relationship "reset" with staff, improved working conditions, workforce planning and pay negotiations.

Source:

Please enter your answer below.

To make sure you answer the question fully, you can copy the requirements into the answer box below using ctrl+c (copy) then ctrl+v (paste) buttons.

Feedback:

Available Answers

- Q1a) (i) (5 Marks)

Available Answers

- Q1a) (ii) (20 Marks)

Available Answers

- Q1b) (5 Marks)

Q1a) (i) Financial Management Implications with respect to volatile funding

Short- and long-term strategic planning is affected by relying on volatile funding streams. Given the **deficit reduction plans** of the 2015 government in the UK, and other similar austerity measures in many other countries, **most public sector organisations have felt the financial squeeze** over the following years. Central government grants can no longer be relied upon for many as 'certain'. This is also the case for many charities and third sector organisations that rely on grants from local government. Financial managers therefore need to be:

- **aware of conditions and performance targets attached to funding;**
- **confident that the risks are being managed around this; and**
- **informed if things are not on track**

The ability to **appropriately plan financially in the short and long term** will rely on innovative financial leaders, capable of supporting the services delivery teams in their organisations.

Especially in times of uncertainty, **financial planning is all about allocating finite resources over time, to reach the broad goals set out in an organisation's corporate or business plan**. It is not enough for financial stewardship to demonstrate that the organisation is financially viable; it **must go on to demonstrate that its activities are financially coherent**.

Budgeting needs to be tied to organisational policy making and strategic planning. Otherwise there becomes a mismatch between what is promised through local and national strategy, and what can be delivered within the financial constraints.

It is necessary for organisations to look at 3-5 year budgeting, and sometimes up to 10 years or more to look at the **longer-term impact that current spending plans may have on the organisation's reserves**.

A Medium-Term Financial Strategy (MTFS but sometimes referred to as Medium-Term Financial Plan - MTFP) supports business planning through **identification of key budgets and the assumptions for change in future years**.

Mark scheme:

Q1a (i) 5 marks for MTFP financial management implications of volatile funding. 1 mark per valid point raised.

Q1a (ii) 20 marks for responses to volatile funding in the public sector. 1 mark per valid point raised.

Q1b 5 marks for building and managing reserves for financial resilience. 1 mark per valid point raised.

Model answer is comprehensive and students are not expected to include all of the detail shown. **Bold text included in answers are the key points to be made.**

Q1a (ii) Responses to Volatile Funding adopted by public sector organisations

Good financial governance

To have any chance of managing volatile funding it is key to have good financial governance arrangements. The publication by Grant Thornton 'Towards the Tipping Point' refers to the risks around volatile funding and states that good financial governance can help mitigate those risks.

The following points are from the Grant Thornton thought-piece and provide a sound reminder list of what good governance looks like across any organisation:

- Regular reporting to the managing body including detail of action planning and variance
- Actions have been taken to address key risk
- The CFO is a key member of the leadership
- Officers and managers across the authority understand the financial implications of current and alternative policies, programmes and
- The leadership ensure appropriate financial skills are in place across all levels of the organisation, for example a good understanding of unit costs and cost
- The leadership foster an open environment of open challenge to financial assumptions and
- There is an effective scheme of delegation, ensuring clarity of financial responsibilities and
- There is engagement with stakeholders, including budget consultations.

- There are comprehensive policies and procedures in place for members, officers and budget holders which clearly outline
- Internal and external audit recommendations are not overdue for implementation.

As well as good governance, there are some specific activities that help financial managers develop solutions to volatile funding.

Managing the risks

As identified above, one of the tools in the solutions box for volatile funding is to manage the risks as effectively as possible. This includes:

- identifying the risky sources of funding
- assessing how likely they are to cease and what the impact of that would be (financially and operationally)
- managing the risks by putting appropriate controls in place to give early warning of potential problems
- mitigating the impact of risks through contingency planning
- monitoring and reporting on compliance with conditions of

Long-term agreements

Using long term agreements can help reduce the risk of volatile funding by building in some certainty to long term financial agreements such as minimum guaranteed funding, and time bound release of funding to match budget cycles.

Financial managers should also seek to influence payments to contractors that limit price rises through the life of the contract, thus reducing the volatility of spending, so that smoothing of budgets can take place where volatile funding is likely.

Diverse sources of income

Financial strategy should ensure that a range of income sources is used wherever possible to help smooth peaks and troughs in funding needs and spread risk of funding loss. Reliance on one source – be it central government or one main benefactor – places an organisation in a much more financially risky position than one that is able to obtain smaller amounts of funding from a range of funding streams.

Seeking opportunities

The most successful organisations that rely on external funding sources are those who:

- keep aware of funding streams available
- have enough resources to seek funding (which can be time consuming)
- complete applications on time, as often the time frame for application can be tight

Examples of local authorities who have a dedicated officer for seeking grant funding from any source demonstrate that they are much more successful in obtaining funding and obtain more funding than those councils who rely on officers applying for grants on a more ad-hoc basis as a small part of their day job. This has been seen in practice, where an external funding officer is employed, and targets are usually set for generating grant income. Charities and third sector organisations employ dedicated staff to generate donations and fundraising and apply for grants.

Mark scheme:

Q1a (i) 5 marks for MTFP financial management implications of volatile funding. 1 mark per valid point raised.

Q1a (ii) 20 marks for responses to volatile funding in the public sector. 1 mark per valid point raised.

Q1b 5 marks for building and managing reserves for financial resilience. 1 mark per valid point raised.

Model answer is comprehensive and students are not expected to include all of the detail shown. Bold text included in answers are the key points to be made.

Q1 b) Why building and managing reserves is critical to ensuring financial resilience in times of austerity

The classification of reserves includes the distinction between useable and non-useable reserves, revenue and capital reserves as well as general and specific reserves.

Managing reserves is a key activity for financial managers in all types of organisations. **Making decisions or recommendations regarding when to hold reserves (and where to invest them), and when to spend, are especially important when formulating strategies to cope with volatile funding.**

A number of high-profile articles have been written in recent years about the level of cash reserves being held by public service organisations – particularly local authorities and the NHS.

Per examples given below, there are differing views on reserves and the levels being maintained by organisations. Prudent financial managers will argue that building reserves is critical to ensuring financial resilience is possible in times of austerity.

Finance managers will ear-mark reserves and ring-fence them for specific projects, set aside monies to cope with a crisis and undertake clever investment to generate income from interest wherever possible. Organisations should also be investigating where investment in assets or projects should be undertaken to generate revenue income going forward.

Public Sector examples on managing reserves

Local Authority example

Councils have been warned by CIPFA that the use of reserves to deal with shortfalls in day-to-day spending would be a 'recipe for significant financial problems'.

Figures published by the Department for Communities and Local Government showed that councils had increased reserves by £2.6bn to £19.1bn in the 2012/13 financial year.

Following publication of the figures, Local Government Secretary Eric Pickles accused councils of 'hypocrisy' over complaints about government funding cuts. Pickles said councils should not be 'pleading poverty' when they were able to increase the money they had saved, and called on town halls to consider whether such substantial reserves were necessary.

But, responding to the figures, CIPFA chief executive Steve Freer said town halls were taking steps to deal with the additional uncertainty of reforms to local government finance.

'Recent changes to local authority funding have created additional uncertainty for councils' future budgets,' Freer said.

'When considered in the context of the government's on-going austerity programmes and ever tighter financial settlements, it is encouraging that the majority of councils are exercising prudence in their reserves management, providing crucial capacity to invest in service transformation and a hedge against future unexpected shortfalls.'

NHS Example

The NHS has pursued a deliberate policy of building up surpluses and then using them in a managed way. It's a complicated system of drawdown, spending limits, estimates and adjustments.

The NHS is facing extreme financial pressures as it looks to meet the challenges of rising demand and expectation within a difficult economic climate. Surpluses built up by commissioners in previous years – as part of a deliberate surplus policy – are being used to help meet some of these pressures while the NHS looks to transform patient pathways.

Mark scheme:

Q1a (i) 5 marks for MTFP financial management implications of volatile funding. 1 mark per valid point raised.

Q1a (ii) 20 marks for responses to volatile funding in the public sector. 1 mark per valid point raised.

Q1b 5 marks for building and managing reserves for financial resilience. 1 mark per valid point raised.

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Fall In Borrowing Offers Chancellor respite

Government borrowing figures have given the chancellor a small glimmer of hope.

Data from the Office for National Statistics (ONS) showed last month that public sector net borrowing excluding public sector banks (PSNB ex) in July 2023 was £4.3bn. It's below the forecast by the Office for Budget Responsibility but still one of the biggest on record.

The ONS explained this was £3.4bn more than that borrowed in July 2022 and is the fifth-highest July borrowing since monthly records began in 1993, behind the pandemic-hit July of 2020 and the three years following the global economic downturn (July 2009, July 2010 and July 2011). The government accounts showed the public sector net borrowing excluding public sector banks (PSNB ex) in the financial year to July 2023 was £56.6bn. That's £13.7bn more than in the same four-month period last year but £11.3bn less than the £68bn forecast by the Office for Budget Responsibility.

The ONS advised against optimism: "July borrowing is typically lower than in most other months because of receipts of self-assessed income tax." But financial markets reacted positively to the figures as a sign that the balance sheet is at least beginning to recover from the financial crisis.

Analysts said there is now more evidence that the economy and government finances are moving in the right direction. An economist at a global accounting firm, said: "Looking ahead, the annual CPI inflation rate continued to fall, reaching 6.8% in July, down by more than 1 percentage point from June. This was the lowest rate since February 2022. Inflation data from recent months meant that the Bank increased interest rates by 25 base points as opposed to a lower hike in their latest interest rate

Please enter your answer below.

To make sure you answer the question fully, you can copy the requirements into the answer box below using ctrl+c (copy) then ctrl+v (paste) buttons.

Feedback:

Available Answers

- Q2a) (i) (10 Marks)

Available Answers

- Q2a) (ii) (3 Marks)

Available Answers

- Q2b) (10 Marks)

Available Answers

- Q2c) (7 Marks)

Model Answer Q2

Syllabus reference: Workbook 1 / A1 and A4, Workbook 5 / A5 and Workbook 4 / A3

Q2a (i) Methods of Government Borrowing

Treasury Bills

Treasury bills are defined as government financial instruments that have a maturity period of less than a year. They are therefore used for short term financing.

Treasury bills are the shortest-term Treasury securities, those that mature within a year (from the time they are issued). The Treasury issues three- and six-month bills every week, and a one-year bill (the so-called 'year bill') once a month. In the UK, the lowest denomination of Treasury bill is £500 000 - in the US, you can buy a T-Bill in denominations of \$100.

Treasury bills are discount instruments. Rather than making interest payments, they are issued at a discount to face value and mature at face value. The interest rate is a function of the purchase price, the face value and the time remaining until maturity.

Bills are quoted in terms of their discount rate, or interest rate based on a 360-day year. As with bond yields, when the discount rate is going up, a bill is losing value. A 'bond-equivalent yield' can be calculated for a bill, to allow for a comparison with other debt instruments.

Government Bonds

Treasury bonds are financial instruments that have a maturity period of more than one year. They are also known as gilts, or gilt-edged securities, in the UK.

Gilts are, very simply, units of debt issued by the government. When buying them, you are effectively lending money to the government, which promises to pay back the amount in full (known as the principal) at a set date, along with interest (known as the coupon).

A conventional 'gilt-edged security' is the simplest and oldest form of government stock. The bond pays out half the annual coupon every six months until the maturity date, when the final coupon payment and principal (the initial investment) are paid to the holder in full.

Gilts are issued at par (UK£100) but are then traded on the open market. This means you can sell the gilt before its redemption date, in which case you might not recoup your initial investment. However, it also means that you can buy gilts below par and hold them until redemption to make a profit. Unsurprisingly, if you buy them above par you can make a capital loss on redemption.

Gilt prices rise when the Bank of England cuts the base interest rate and fall when the base rate goes up. So gilt yields rise and fall with interest rates. This is one of the great attractions of conventional gilts; you can lock into a high yield that will be maintained no matter how far rates subsequently fall.

Gilt prices are also affected by the market's perception of future interest rates, and this is reflected in the yield curve. The longer a gilt has to maturity, the more sensitive it is to changes in interest rates – something known as duration risk.

For both bonds and treasury bills, these may be traded, but will only rarely be spent on goods and services. In this way, the expected increase in inflation due to the increase in national wealth is lower than if the government had simply printed the money and increased the more liquid forms of wealth (i.e., the money supply).

National Savings

A state bank is generally a financial institution that is chartered by a state. It differs from a reserve bank in that it does not necessarily control monetary policy (indeed, the state in question may have no legal capacity to create monetary policy), but instead usually offers only retail and commercial services. Here are two examples:

Example of National Savings - NS&I (UK)

National savings and investments (NS&I) is the UK government agency that is responsible for managing and obtaining domestic investment. Formerly called the Post Office Savings Bank and National Savings, it is a state-owned savings bank in the United Kingdom. It is both a non-ministerial government department and an executive agency of the Chancellor of the Exchequer.

Historically, the aim of NS&I has been to attract funds from individual savers in the UK for the purpose of funding the government's net cash requirement (i.e., the funds in excess of taxation that the government requires to fund its expenditure). NS&I attracts savers through offering savings products with tax-free elements on some products and a 100% guarantee from H.M. Treasury on all deposits. However, its interest rates are often low.

Premium Bonds can also be purchased from NS&I. These are personal investments in units of £1, for a minimum value of £100, with a maximum investment of £50 000. The investment is 100% guaranteed and can be withdrawn with no notice or penalty, but no interest is paid on the investment.

Instead, the Premium Bond numbers are entered into a monthly draw (like a lottery), and winners receive prizes ranging from £25 to £1 million – tax free. The chances of winning large prizes are very small (1 in 36 billion of winning £1 million for each £1 stake), and statistically, the average pay-out is less than would be received if you left your money in a regular interest-bearing account for a year.

They are recommended to individuals who wish to invest with no risk and have reached their maximum deposits with other tax-free investments. They are, however, a useful source of borrowing for the government, as mostly they are long-term deposits.

Examples of National Savings - Sparkassen-Finanzgruppe (Germany)

The German Savings Banks Finance Group (Sparkassen-Finanzgruppe) is the most numerous sub-sector with 431 savings banks using the Sparkasse brand, 8 Landesbanken (including the DekaBank) using separate brands and 10 real estate financing banks using the LBS brand. The Deutscher Sparkassen- und Giroverband (German Savings Banks Association, DSGV) represents the interests of the Sparkassen-Finanzgruppe on a national and international level concerning law and the financial services industry. It also coordinates, promotes and harmonises the interests of Sparkassen.

Based on OECD studies, the German public banking system had a share of 40% of total banking assets in Germany. This shows the important and significant role of this group of banks in Germany.

Certificates of tax deposit

In the UK, the Certificate of Tax Deposit (CTD) scheme allowed you to deposit money with HM Revenue and Customs (HMRC) and use it later to pay certain tax liabilities. Deposits with HMRC earned daily interest for up to 6 years. In this way, the government was effectively borrowing funds from the depositor and aiding the government's cash-flow, until the liabilities were paid.

From 23 November 2017 this scheme has been closed for new purchases but existing certificates were to be honoured until 23 November 2023.

2 a (ii) Domestic versus Foreign Debt

Domestic Debt

This is also known as internal debt and arises where a government borrows money from lenders within its own country. Domestic (or internal) public debt is where the citizens of that country (as opposed to financial institutions) lend money to the government (in the form of securities such as bonds or treasury bills).

When debt is financed domestically, there is an argument that it may 'crowd out' the private sector as there might be an increase in the interest rate and the cost of borrowing for the private sector (or directly limits availability of finance in developing countries). This would clearly have a negative impact on the economy of a country and could hold back growth.

Foreign Debt

By borrowing from overseas, governments can bring more investment into the country, thereby reducing the crowding out impact. This is known as Foreign (or External) Debt. Most national governments will have a combination of foreign and domestic debt.

Interest on foreign debt does leak from the economy. Government bonds are usually denominated in the home currency, but in some cases, particularly in developing countries, these are often denominated in foreign currencies (such as the US Dollar), which carry significant exchange rate risks.

Mark scheme:

2 a (i) 20 marks for methods of government borrowing – treasury bills (2 marks), government bonds (2 marks), national savings with an example (4 marks of which 2 marks are for the example) and certificates of tax deposits (2 marks).

2 a (ii) 3 marks for distinguishing between domestic and foreign debt. 1 mark per valid point raised.

(13 marks)

Model answer is comprehensive and students are not expected to include all of the detail outlined.

Q2b) Arguments for the advantages of Public Finance Initiatives

Proponents argue the following advantages of PFI:

PFI offer better value for money than state financed capital investment

Risk is transferred from the public to the private sector and the value of the reduced risk should be included in the comparison of the relative costs of Public Private Partnerships (PPP) and public funding

Using private finance reduces public borrowing

Long contracts (25-35 years) provide predictability of service

Responsibility for staff and associated risks of providing services transfers to the private sector

Opponents argue the following disadvantages of PFI:

The cost of capital is higher (private sector interest rates are higher than those on government debt)

In practice risk is not transferred, since governments cannot afford to let major projects fail, so the value of the risk reduction is not a relevant cost factor

The cost of the capital expenditure is borne by the public finances, but through lease arrangements, and in any case that cost is likely to be higher than through public borrowing

Government is locked into a pattern of service provision implied by the use of the building and technology may change before the period of the contract ends

The arrangement leads to lower pay and less favourable conditions for workers. This can lead to staff shortages and an inability to provide services at the levels contracted for

Mark scheme:

1 mark for each point raised per mark scheme, up to 5 marks for advantages and 5 marks for disadvantages of PFI. (Maximum 10 marks)

Model answer is precise and students are expected to include all of the detail.

Q2c). Local sources of taxation for public services

Property taxes:

Property is the classic immobile asset and most local taxation authorities will use property taxes as a key element in their revenue portfolio. Whilst the asset is not portable, where people choose to live is discretionary. The level of taxes levied on property therefore will potentially have an impact on the price of the asset. Put simply, higher property taxes will reduce house prices in an area provided all other factors are equal.

User charges/fees:

Beneficiaries of delivered services pay directly for them (not necessarily full cost).

Examples of this approach are numerous including sports facilities, utility consumption, waste collection, crematoria, car parking and social housing. These are clearly located in a community setting and are therefore not mobile. There is an advantage also that where non-residents can use the facilities it reduces the impact on residents of neighbouring authorities free riding on the facilities. This can often be a problem of urban authorities with a large population which provide services in towns and cities that surrounding, less populous, rural authorities may not be able to provide cost effectively.

License fees:

These are primarily intended to contribute towards the administration of such regulatory activities as business & driving licences, registration fees and drink or entertainment licences. For example if, for public health reasons, food establishments have to be inspected then a licence fee is a useful method to ensure that the premises are registered, that they are inspected regularly and if health dangers are found they can be corrected or the business closed down. The licence fee is again immobile.

Levies on properties for infrastructure improvement:

This is similar to the levying of property taxes and can be on households or businesses. The money raised is usually ring-fenced to finance improvements in such things as public transport systems, broadband access or off-street parking in shopping areas.

National taxes:

In many countries there is a tax sharing system whereby a certain proportion of national taxes, for example VAT, are retained locally. This has the advantage that local economic activity is rewarded with a share of revenue thereby encouraging the local authority to develop the local economy more effectively. It can of course sometimes lead to tax competition, for example, out of town shopping malls being located on the border of a neighbouring local authority.

Mark scheme:

1 mark for each point raised per mark scheme, with up to 7 marks for 3 examples given.

Model answer is comprehensive and students are not expected to include all of the detail.

**Requirement****Q3a)**

Justify why business cases are important in public sector organisations. (5 marks)

Q3b)

Identify and describe the five 'cases' or 'dimensions' that must be evidenced in a business case in support of a new policy, strategy, programme or project. (5 marks)

Total: 10 Marks

Please enter your answer below.

To make sure you answer the question fully, you can copy the requirements into the answer box below using ctrl+c (copy) then ctrl+v (paste) buttons.

Feedback:**Available Answers**

- Q3a) (5 Marks)

Available Answers

- Q3b) (5 Marks)

Model Answer Q3

Syllabus reference: **Workbook 11 / C2**

1. Why Business Cases are important in public sector organisations

Business cases are important because policies, strategies, programmes and projects will only achieve their spending objectives and deliver benefits if they have been:

- **scoped robustly**
- **planned realistically** from the outset
- **the associated risks and costs have been taken into**

The business case, both as a product and a process, **provides decision makers, stakeholders and the public with a management tool for evidence based and transparent decision-making, and a framework for the delivery, management and performance monitoring of the resultant scheme.**

1. Five 'cases' or 'dimensions' that must be evidenced in a business case

The business case in support of a new policy, new strategy, new programme or new project must evidence the five 'cases' or 'dimensions', namely:

- the **strategic case**: intervention is supported by a compelling case for change that provides holistic fit with other parts of the organisation and public sector
- the **economic case**: intervention represent best public value
- the **commercial case**: the proposed deal is attractive to the market place, can be procured and is commercially viable
- the **financial case**: the proposed spend is affordable
- the **management case**: what is required from all parties is achievable

Mark Scheme:

a). 5 marks: 1 mark per valid point

b). 5 marks: 1 mark for identifying each case and 1 mark for describing it adequately

Maximum 10 marks

Model answer is precise and students are expected to include all detail shown.



Governance arrangements for collaboration in the public sector should be effective enough to ensure transparency in decision-making and actions taken, without interfering with service delivery to the customer.

Requirement**Q4)**

Present the fundamental elements of good governance that can apply to any shared working arrangement in the public sector.

(10 marks)

Total: 10 Marks

Please enter your answer below.

To make sure you answer the question fully, you can copy the requirements into the answer box below using ctrl+c (copy) then ctrl+v (paste) buttons.

Feedback:**Available Answers**

- Q4) (10 Marks)

Model Answer Q4

Syllabus reference: Workbook 12 / C4

Fundamental elements of good governance that can apply to any shared working arrangement in the public sector.

Shared understanding

Partners should formally agree and record how a partnership operates, including:

- structure
- purpose and aims
- activities
- roles and responsibilities
- membership
- regulatory framework
- exit

Accountability

Partnerships should account for actions through:

- reporting, meetings
- oversight and scrutiny of performance and regulatory compliance
- openness and engagement
- complaints and redress

Decision-making

There should be clearly allocated roles, responsibilities, accountabilities and open and transparent processes, such as:

- records of delegated authority and key decisions
- effective

Value for money

Costs and benefits should be understood to ensure arrangement provide value for money over alternative arrangements.

Corporate governance processes

Good governance contributes to delivering high-quality, cost-effective services through effective systems and process for managing issues, such as risk (including insurable risk) performance, finance and information.

Standards of conduct and leadership

High standards should be agreed to govern the way the partnership works, to ensure the needs of all partners are met, to identify conflicts of interest and to resolve disputes.

Mark scheme:

10 marks – Shared Understanding (2 marks), Accountability (2 marks), Decision-making (2 marks), Value for Money (1 mark), Corporate governance processes (2 marks) and Standards of conduct & leadership (1 mark).

Maximum 10 marks. Model answer is precise and students are expected to include most of the detail. Use bold highlight as a guide for marks.



Risk aversion is commonplace in public sector organisations.

Q5a)

(i) Explain why risk aversion is expected in the public sector. (2 marks)

(ii) Give an example of a high-profile event that helped shape public awareness of treasury risks over the last 20 years. (3 marks)

(5 Marks)

Q5b)

Risk assessment should be undertaken at various stages in the business case development.

Describe each of the following risk categories when they are assessed in a business case for a public sector organisation:

- (i) Business Risks (2 marks)
- (ii) Service Risks (2 marks)
- (iii) External environmental risks (1 mark)

(5 Marks)

Total: 10 Marks

Please enter your answer below.

To make sure you answer the question fully, you can copy the requirements into the answer box below using ctrl+c (copy) then ctrl+v (paste) buttons.

Feedback:**Available Answers**

- Q5a) (i) (2 Marks)

Available Answers

- Q5a) (ii) (3 Marks)

Available Answers

- Q5b) (5 Marks)

Model Answer Q5

5a) (i) Why Risk Aversion in the Public Sector is commonplace

Some reasons for risk aversion include the sense of stewardship for public funds or the unacceptable consequences to service delivery that might be caused by a loss on an investment. Some reasons are more political, such as fear of criticism.

Mark scheme:

-

5 marks: 2 marks for why risk aversion in the public sector is commonplace (reasons for) and 3 marks for an example of a high-profile event that helped shape public awareness of treasury risks over past decades.

5 marks: Describe risks assessed in a business – Business risk (2 marks), Service risks (2 marks) and External environmental risks (1 mark)

Maximum 10 marks

Model answer is comprehensive and students are not expected to include all of the detail shown above but should demonstrate their understanding of topic being tested. Bold highlighted content is critical for inclusion.

5 a) (ii) Some Examples of high-profile events that helped shape public awareness of treasury risks

Public awareness of treasury risks has been shaped over the last couple of decades by high profile events including:

1. Collapse of the Bank of Credit and Commerce International (BCCI) in 1990
 2. Controversy over interest rate swaps
- Collapse of the Icelandic banks

BCCI impact

The Bank of Credit and Commerce International (BCCI) was a major international bank founded in London in 1972. At its peak it was the 7th largest bank in the world by assets.

In 1991 regulators in the United States and the United Kingdom found it to be involved in money laundering and a range of other illegal activities. The bank was found to have at least 13 billion US dollars unaccounted for. It was forced into liquidation.

A number of local authorities in the UK lost significant sums of money as a result, which was one of the factors leading to the development of clearer guidance for public sector treasury managers.

Interest rate swaps

The Hammersmith and Fulham case is a high-profile case where, in 1991, the courts ruled local authorities did not have powers to use particular capital market instruments, particularly interest rate swaps.

Where it all went wrong for Hammersmith and Fulham is that they were running a swap book for speculative purposes rather than to hedge against interest rate changes on an underlying loan. They carried out only the fixed/floating swap part of the transaction without doing the first stage of borrowing an amount of principal from a bank because there was a real need.

The swaps thus became a gamble on interest rates. The treasury managers at Hammersmith and Fulham got out of their depth because they did not understand the full extent of their potential losses on their swap book.

When the banks asked for their money, Hammersmith and Fulham attempted to avoid their liabilities by claiming that they did not have any powers under local government legislation to enter into contracts of a speculative nature. The High Court originally ruled against them and in favour of the banks but the case was appealed. In the end the Court of Appeal ruled that the swaps were ultra vires (beyond the authority's legal power) and therefore the banking counterparties ended up having to cover the losses.

The Icelandic banks

The uncertainties and volatility in financial markets (commonly called the 'credit crunch') and specific examples such as public sector organisations that invested surplus cash in failing Icelandic banks, have meant that although value for money is sought in treasury management, the focus on risk versus return has become even more important.

Local authorities had nearly £1bn invested in Icelandic banks when the banks went into administration. Many analysts felt that the Icelandic banking crisis was foreseeable and that public bodies should have acted before the full crisis hit.

Following the Icelandic crisis, a widespread reaction was observed in local authorities and other public bodies: counterparty lists were drastically reduced and limits tightened. Risk of experiencing default was in most cases reduced; however return certainly was.

Mark scheme:

-

5 marks: 2 marks for why risk aversion in the public sector is commonplace (reasons for) and 3 marks for an example of a high-profile event that helped shape public awareness of treasury risks over past decades.

5 marks: Describe risks assessed in a business – Business risk (2 marks), Service risks (2 marks) and External environmental risks (1 mark)

Maximum 10 marks

Model answer is comprehensive and students are not expected to include all of the detail shown above but should demonstrate their understanding of topic being tested. Bold highlighted content is critical for inclusion.

5b) Describe risks that are assessed in a business case for a public sector organisation.

Risk categories	Description
Business risks	Strategic risks which remain (100%) with the public sector organisation regardless of the sourcing method for the proposed spending. They include political risks .
Service risks	Risks associated with the design, build, financing and operational (DBFO) phases of the proposed spending . They can be shared with business partners and service providers.
External environmental risks	Risks that affect all organisations regardless of whether they are public or private sector. They include secondary legislation and general inflation.

Mark scheme:

-

5 marks: 2 marks for why risk aversion in the public sector is commonplace (reasons for) and 3 marks for an example of a high-profile event that helped shape public awareness of treasury risks over past decades.

5 marks: Describe risks assessed in a business – Business risk (2 marks), Service risks (2 marks) and External environmental risks (1 mark)

Maximum 10 marks

Model answer is comprehensive and students are not expected to include all of the detail shown above but should demonstrate their understanding of topic being tested. **Bold highlighted content is critical for inclusion.**



Benchmarking can be a key element of measuring performance and success.

Q6a)

Define benchmarking, and the main objectives of undertaking benchmarking in the public sector.

(3 marks)

Q6b)

The use of benchmarking 'families' in the public sector is common. Discuss the factors to be considered when choosing benchmarking families.

(7 marks)

Total: 10 Marks

Please enter your answer below.

To make sure you answer the question fully, you can copy the requirements into the answer box below using ctrl+c (copy) then ctrl+v (paste) buttons.

Feedback:**Available Answers**

- Q6a) (3 Marks)

Available Answers

- Q6b) (7 Marks)

Model Answer Q6

Syllabus reference: **Workbook W13 / C5**

Q6)**Definition of Benchmarking**

Benchmarking can be defined as:

'the measurement (of the quality / efficiency /effectiveness) of an organisation's policies, performance, strategies, costs, etc., and their comparison with standard measurements, or similar measurements of its peers'.

The objectives of benchmarking are:

- to determine what and where improvements are called for
- to analyse how other organisations achieve high performance levels
- to use this information to improve

Benchmarking Families (Who to benchmark with)

When considering benchmarking, the choice of comparators is important and should be the organisations that will give the most informative and relevant comparison.

For example, many organisations in local government could benchmark with their geographical neighbours, when the demographics of those neighbours may be very different. A better comparison could be those local authorities with a similar demographic profile.

Factors to consider when choosing benchmarking 'families' are:

- organisation type / sector
- organisation size
- size and nature of the area covered by the organisation
- demographics
- geographical location
- strategic / policy approach

Looking at each of these **factors** in turn:

Organisation type / sector

Most organisations will wish to compare themselves with others who operate in the same sphere as themselves – housing, hospitals, police forces, etc.

The advantage of this approach is that there may already be contacts across that sector and there will be information readily available to be shared.

For example, for Police, Her Majesty's Inspectorate of Constabularies (HMIC) produce annual profiles which compare performance and data from all Police Forces in England & Wales. Similarly, CIPFA produce a wide range of statistics for public sector organisations, featuring all those who participate in the data collection exercises.

A disadvantage of these sector-specific comparisons is that if the sector as a whole is not performing as well as it should, the value of benchmarking for improvement will be limited. Consider whether your own organisation would want to promote itself as being 'one of the best of a bad bunch'? In these circumstances, some comparisons outside the sector – with other organisations that share similar characteristics – could be more useful.

Organisation size

Whilst many performance measures are taken as a unit cost or a cost per head of population, rather than absolute values, there may still be differences due to the size of an organisation. Factors such as economies of scale, purchasing power and influence may mean that comparisons between a small organisation and a much larger one are not valid.

When establishing a group of suitable peers to be in a benchmarking group it is advisable to look at the number of employees, overall budget and the population served.

Size / Nature of area covered by an organisation

Undertaking benchmarking comparisons between an organisation serving a large urban population and one serving a small, spread-out rural population would not give the best results – the needs of clients (and the ability to deliver services) will be very, very different.

Demographics

In a similar way, the needs of a population that is served by an organisation can be very different due to demographics. A well-off, wealthy but primarily elderly area will have a set of needs that do not match those of an area with more young people, with high levels of deprivation and poverty, and it follows that the organisations serving these areas will be different too.

Geographical location

For the same reasons as for demographics and size of area, geographic areas can be a factor to consider in benchmarking. In some cases, comparing performance with its nearest neighbours can be the best option for an organisation, especially if the geography does affect service levels, demand and cost.

Clearly, this is also a factor when considering international or global comparisons.

Strategic / Policy approach

Organisations that take the same position on service delivery can make good and useful comparators. For example, looking at other organisations which have adopted an outsourcing approach for back-office services would be a suitable approach for an organisation which has contracted out its Finance, HR and ICT functions.

Mark scheme:

3 marks for Benchmarking definition (1 mark) and objectives (2 marks)

7 marks for Benchmarking families/ factors explained adequately

Maximum 10 marks

Model answer is comprehensive and students are not expected to include all of the detail in mark scheme. Bold highlighted content is critical for inclusion and explanation.