FINANCIAL GOVERNANCE IN THE NHS

Are we getting the best bang for our buck?

The use of run rates is simplistic to model yet is a great way of comparing prior/current and future year projections and understanding key movements and assumptions. All too often this simplistic approach is not adopted and boards are unsighted on run rate projections both at the time of signing off financial plans for the forthcoming year and in relation to in-year monitoring of financial performance; avoiding fundamental planning deficiencies, including, for example, not budgeting for a level of temporary staffing spend which is appropriate based on current or historical run rates and known recruitment plans. Boards should scrutinise anticipated projections in such political and volatile areas of spend and challenge assumptions prior to sign off of the financial plan; and

a clear audit trail which allows the board and organisation to understand how the new budget relates to the previous year and a robust change control process to ensure understanding at every stage of the process. This will minimise the likelihood of making poor decisions on inaccurate data.
FOREWORD

With an overall deficit of £2.45bn the state and profile of the NHS sectors’ finances is at its highest level for a generation. It is critical that all NHS organisations maintain tight financial control and that they do everything possible to stop a ‘deficit blind’ organisational cultural malaise from developing.

The number of instances where NHS provider financial performance has deteriorated rapidly and dramatically has increased significantly. Whilst everyone would recognise the multifactorial nature of many of the causes of this, there remains, from our experience, criticisms of the robustness and focus locally on how NHS providers manage their finances.

We have conducted a number of independent reviews into the causes of adverse financial performance in the NHS sector, and have, on each occasion found many of the causes to be known national drivers, such as the cost of temporary staffing, delayed discharges and impacts of national tariff constraints. However, we have also found that organisations themselves are increasingly tolerant of growing deficits, too readily accepting that ‘everyone is running in the pack’, and as deficits grow, are becoming less focused on core financial management controls and choosing to externalise the issue without ensuring that their own organisation effectively manages its own finances.

Whilst undoubtedly there are significant system wide and national level issues to tackle, in this document we discuss a number of simple quick wins and improvements that can be made at an organisation level to recover local control of your organisation’s finances. Whilst these alone will not eradicate the NHS’ financial problem, they will contribute to stemming the flow and help instill effective financial control into NHS providers. Otherwise we run the very real risk of losing financial discipline and creating a financial culture which will be even harder to turnaround.

Mike Gill, Director, Consulting, RSM
The majority of organisations commence their financial planning process in the autumn of the preceding year and invariably have a comprehensive plan in place with milestones, accountabilities, clearly marked dependencies and sign off arrangements agreed. Their plans demonstrate a high level of clinical and operational engagement, appropriate senior challenge and board level approval.

However, as the financial planning timetable progresses and winter sets in, organisations typically become side tracked by operational and financial issues which often result in an increased focus on delivering an acceptable and often negotiated year end control total. The well-constructed financial planning timetable can soon become a distant memory.

There are some organisations though who successfully manage to balance the need for operational financial oversight with robust financial planning and they are able to deliver all or most of the positive elements included within their financial plans. The key elements of an effective planning process are:

1. A clear and comprehensive financial planning schedule which encompasses all the key aspects of financial planning including milestones, accountabilities, dependencies, outputs and sign off arrangements;
2. A clear framework (or ‘rules’) that set out the corporate expectations in relation to inflationary impacts, activity volumes, efficiency requirements, treatment of vacancies and business cases;
3. Using financial and business planning templates, ensuring greater consistency of format and quality, reducing the margin of error in aggregation and understanding;
4. A clear expectation of the level and breadth of operational and clinical engagement and inclusion in developing and agreeing local sign off of plans in addition to the authorisation and corporate sign off processes thus ensuring local ownership and buy-in;
5. Continued dialogue and iteration throughout contract negotiations with commissioners as required activity volumes are firmed up. This is vital in securing local ownership throughout the financial planning process and not just at the draft stage. Too often the draft plans are taken into the centre around late December/early January and by the conclusion of the contract income negotiations with commissioners, the required activity volumes can look significantly different to those developed locally. This ‘disconnect’ often leaves budget holders disengaged, frustrated and lacking in motivation to deliver a financial plan that they do not recognise nor own. Indeed, in our reviews we have found devolved entity budgets not signed off due to disagreements and yet the board remained unsighted on such issues when it formally approved the overall financial plan for the year ahead;
6. The use of benchmarking data or prior year run rates to help to sense check and challenge assumptions where necessary. The use of run rates is simplistic to model yet is a great way of comparing prior/current and future year projections and understanding key movements and assumptions. All too often this simplistic approach is not adopted and boards are unsighted on run rate projections both at the time of signing off financial plans for the forthcoming year and in relation to in-year monitoring of financial performance;

7. Avoiding fundamental planning deficiencies, including, for example, not budgeting for a level of temporary staffing spend which is appropriate based on current or historical run rates and known recruitment plans. Boards should scrutinise anticipated projections in such political and volatile areas of spend and challenge assumptions prior to sign off of the financial plan; and

8. A clear audit trail which allows the board and organisation to understand how the new budget relates to the previous year and a robust change control process to ensure understanding at every stage of the process. This will minimise the likelihood of making poor decisions on inaccurate data.
Once the annual budget has been set and approved in advance of the financial year, our attention turns to how this is monitored and managed in-year. The quality of the discussions and challenge will only ever be as good as the quality of the financial reporting. This is true irrespective of the level within the organisation at which you wish to hold such discussions.

The basic fundamentals of good quality reporting are the same whether or not it is financial or non-financial information being reported. These include:

1. accurate and meaningful data that the recipient can understand and believe in;
2. timely data and discussion; considerable effort is put in to ensuring that financial reporting is available by working day five or six after the period end, which is good practice, however as a result discussions are often not held with budget holders until much later in the month, negating the benefit of reporting in a timely fashion;
3. finance reports should be action oriented and not too discursive. A balance needs to be struck between reporting the current position and ‘why we are where we are’, and being forward looking and providing assurances in relation to the ‘so what are we doing about it’ question. All too often reports are imbalanced towards reporting the current financial position;
4. the use of trend data, run rates, forward projections and trajectories which all provide the reader of the financial report with more rounded information to better understand the current performance relative to recent performance. This also provides the opportunity to test the validity of existing forecasts, challenge assumptions and monitor the success or not of planned actions to deliver the financial plan or recover an adverse variance;
5. the use of RAG reporting or other visual aids to focus the reader on those areas of greatest concern. A good finance report will direct the reader to the key issues of concern and focus — ensuring discussions remain relevant and set out what is being done to address concerns;
6 the reporting of actions which include timescales, accountabilities, expected impact and monitoring arrangements to help the reader gain assurance that the organisation is responding to the key issues. This creates a good basis for ongoing monitoring of the impact of such actions and whether or not they are sufficient to address the issue;

7 it is essential that organisations do not too rigidly follow historic reporting templates. When variances arise, it is important that the finance report reflects areas of emerging or increasing concern and include deep dive analytical analysis. This will provide the reader with greater understanding behind the main causes of the variance(s) and the key drivers, identifying those areas to be tackled and monitored going forward; and

8 the finance report should incorporate balance sheet and other non I&E reporting to provide rounded assurances over the overall financial health of the organisation. In recent high profile examples where NHS organisations were perceived to have lost financial control, the relative health of the balance sheet and in particular the cash levels and one off movements out of reserves could have raised more timely concerns regarding the underlying financial position. Cash is a good barometer of financial health and the inclusion of such matters at finance committee level financial reporting is essential to provide the necessary level of assurance.
The ever increasing financial challenge coupled with the need to deliver appropriate services to an ageing and growing population, makes it more important than ever for Trusts to retain effective oversight of the planning and execution of cost improvement plans (CIPs).

Through our work with the sector we still experience organisations whose centralised planning, lack of challenge and poor reporting, result in a failure to address some of the basic financial management principles which will help deliver improved performance. We discuss some of these points opposite.

1. Many CIP schemes are top down driven and based on statistics and do not reflect the individual organisations start point, culture and resources. It is therefore not surprising that they fall short of delivering the expected benefits derived from the desk top analysis. It is important that any such analysis is seen as the maximum potential benefit and that local considerations are taken into account to produce a realistic and achievable target.

2. Insufficient clinical engagement and a lack of peer challenge can adversely impact on local ownership and buy-in or impact adversely in other areas via unintended consequences. This is often due to a failure to adequately build in time for peer level engagement and local clinical sign off by the teams responsible for actually delivering the change.

3. Quality Impact Assessments (QIAs) need to be undertaken prior to commencement of the CIP scheme implementation and ideally prior to the commencement of the financial year. QIAs should be in place for all required schemes prior to the Board’s approval of the financial plan at the start of the year. Otherwise Boards are unsighted on the potential impact on quality when approving the associated CIP plans contained within the overall financial plan. We still see instances occurring where QIA sign off is happening some months into the financial year.

4. When Boards are approving annual financial plans it is important that each member of the Board understands the plan and that they have assurance over how the Trust is expecting to deliver the plan. This level of scrutiny as a minimum should include sample testing of detailed plans relating to some of the more significant CIP schemes. Our experiences show that some organisations are too reliant upon verbal reassurance from executive directors at the point of sign off as opposed to undertaking appropriate scrutiny.

5. Trust should be mindful of the pitfalls relating to the back loading the CIP plan and then leaving minimal time to respond should the CIP plan not deliver as per expectations. Part of the consideration and challenge by the Board is to ensure that CIP planning commences early in the financial planning cycle and that a suitable proportion of the plan value is scheduled to deliver in the early part of the year. This provides more time for escalation and additional actions should the plan not deliver as per expectations.

6. There should be clear executive responsibility for each significant scheme identified in addition to local management and an overall executive sponsor for the whole programme. The executive sponsor should be responsible for the delivery and reporting of the programme and overseeing and ensuring delivery of individual schemes;
Once approved and started it is important that the CIP programme is reported in sufficient detail in order to provide assurance and allow for challenge where adverse variances are occurring. This requires the programme to be reported at individual scheme level alongside the expected timeline of savings, and preferably in a visual way to complement the tabular numbers and percentages being reported. Schemes should be RAG rated based on delivery performance to draw the reader to those individual schemes of concern;

CIP reporting should also differentiate between recurrent and non-recurrent savings so that Board members are sighted on the balance between the two. This then gives them the opportunity to challenge savings if it is felt there is an over reliance on non-recurrent measures to deliver in-year requirements.

Where transformational CIP schemes that will have an impact across several reporting entities are planned, it is important that there are clearly identified accountability arrangements in place. Joint arrangements invariably result in confusion and distraction and make it difficult to hold the appropriate person to account for delivery. Equally, reporting of such arrangements must be agreed prior to the commencement of the scheme and as part of the overall planning considerations. Proportionate savings across multiple reporting entities should be avoided wherever possible.

Where individual schemes are off track the report should include detail of the actions (including responsibility and timeline) being taken to improve performance alongside any revised delivery timelines and values. This allows the reader to track the implementation and impact of each action and be sighted on the overall revised value and timeline for delivery of the whole programme.

From our findings there is a clear need for an executive led CIP oversight group which meets regularly. Frequency should be flexed to reflect the success or not of current delivery and may require weekly or fortnightly frequency at time of significant variance to plan. The membership of the group should incorporate senior clinical and operational personnel in addition to executive and corporate leads.

Inevitably there be wil schemes that under deliver due to a combination of over estimation of the value or slippage in implementation timelines. Therefore it is important to ensure that the organisation has a ‘reserve’ of potential schemes that can be expedited as required or that the organisation employs a continual planning approach to CIPs as and when opportunities arise, as opposed to undertaking an annual cycle of identification, planning and delivery.
It is essential that an organisation deploys robust financial management at all levels. Back office cut backs and re-organisations have left some organisations with stretched resources to undertake even the most basic elements of good financial management. This dilution in operational level financial management can lead to deterioration in skills at a local level, inaccurate budget statements due to poor communications and relationships which stem from a lack of routine engagement. Once the low level operational budgets become inaccurate and unrecognisable the ownership and motivation to hold to account diminishes to the point where there is ineffectual local grip on the finances.

An enabler of robust financial management is having a high level of financial literacy within an organisation. Financial budgetary training and financial awareness sessions support and develop individuals to understand, interpret and respond to the financial information being presented to them. The ability for organisations to resource a programme of financial training is often more limited now than in previous years as a result of corporate cost savings, and this has meant many new operational management appointments have not received even basic financial training.

This equally applies to middle and senior level management teams who are often appointed into their first managerial post without adequate investment and training in the corporate elements of their responsibilities. This lack of financial literacy coupled with reductions in financial management resources can result in a diminished understanding of organisational finances and therefore their ability to adequately understand and control it.

At divisional level there is the need for regular monthly reviews of performance which should incorporate financial performance as part of a balanced scorecard conversation. There needs to be an appropriate membership for the reviews to ensure sufficiently detailed conversations and challenge take place. Discussions need to be supported by appropriate financial reporting which adheres to the good practice principles as set out in section two of this document.

We find that operational pressures lead to this level of meeting being all too often cancelled or cut short or alternatively sporadic attendance leading to ineffectual discussions, decisions and follow through. These meetings are, in reality, the main interactions between the corporate body and the operational structure of the organisation and the mechanism by which the corporate centre holds to account the rest of the organisation. Less than effective meetings at this level, in our opinion, are a major cause of overall poor performance and disconnection within an organisation. When conducted well these meetings contribute to the overall health, positive culture and consistency of approach and invariably supports improved performance.

The majority of organisations operate a finance committee which reflects the increasing financial challenge and the need for ring fenced time to scrutinise and discuss financial matters at Board level in greater detail. An effective finance committee is suitably focused and supported by appropriate reporting with a culture of constructive challenge and should be a value adding part of the overall financial management arrangements within an organisation. However, finance committees should not be seen as an additional layer of executive delivery management. Such committees are designed to be an additional layer of scrutiny, assurance and challenge operating as an extension of the Board ie assurance driven not delivery led.

Within our work we have identified instances where organisations blur the lines of accountability and cause confusion by inviting divisions to attend and present their financial position to the finance committee allowing the committee to hold the divisions to account for delivery of their finances which is an executive function. This duplication of role can create confusion within an organisation and dilute the ability of the Board to hold executives to account over delivery as in effect the committee has taken on that role.
Essential to the successful operation of a finance committee is the ability to spend time drilling down in detail into the main adverse variances and gaining a deeper understanding of the key drivers and mitigations. This will require an agile agenda capable of being flexed to respond to emerging issues and being risk based and not rigid. The ability to delve into the detail requires an additional layer of reporting beyond that normally delivered at Board level and it is important that organisations recognise this and provide differential reporting to the finance committee and the Board. Similar or same financial reporting will invariably lead to similar or same discussions being had in both forums.

Understanding the purpose of financial reporting and reflecting on what the reader at each level requires should help inform the development of fit for purpose financial reporting. We have covered the good practice reporting principles within section two of this document and summarise below the key elements by level:

### LEVEL

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<thead>
<tr>
<th>LEVEL</th>
<th>KEY ELEMENTS</th>
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<tbody>
<tr>
<td>Ward/department</td>
<td>• Accurate and timely budget statements</td>
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<tr>
<td></td>
<td>• Analysis of key variances and movements in period</td>
</tr>
<tr>
<td></td>
<td>• Agreed budget architecture and hierarchy</td>
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<tr>
<td>Directorate/division</td>
<td>• Use of trends and analytical forward projections</td>
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<tr>
<td>(as above +)</td>
<td>• Use of deep dive analysis, benchmarking and comparators of key drivers of variances</td>
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<tr>
<td></td>
<td>• Use of SLR/PLICS to report rounded I&amp;E performance</td>
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<tr>
<td>Finance committee</td>
<td>• Greater use of aggregation and summaries</td>
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<tr>
<td></td>
<td>• Greater use of tables, graphs and visual formats to convey key messages</td>
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<tr>
<td></td>
<td>• Use of appendices to aid reporting at granular level of detail and deep dive analysis to support organisational wide key variances and drivers</td>
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<tr>
<td></td>
<td>• Greater use of forward looking reporting and risk based outturn projections to inform best/likely/worse case scenarios</td>
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<td></td>
<td>• Greater emphasis on actions and mitigations of key variances and projected impacts/timelines</td>
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<tr>
<td></td>
<td>• Increased use of benchmarking and inclusion of external factors</td>
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<td></td>
<td>• Inclusion of rolling cash flow forecasts, reserve movements and debtor/creditor value trends as useful barometers of financial health</td>
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<tr>
<td>Board</td>
<td>• Similar core financial report as the finance committee albeit excluding many/all of the appendices</td>
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<tr>
<td></td>
<td>• Report supported by the outcome and minutes from the latest finance committee which sets out actions taken, assurances provided and risks identified</td>
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We appointed RSM to complete an independent assessment of the robustness of our revised financial projections. In particular this was to provide assurance, or otherwise, to the Board and the TDA that the revised projections were robust.

RSM did a speedy and very credible piece of work. The team immediately demonstrated an experienced grasp of the key issues and a strong knowledge around the more technical issues. They produced a coherent and comprehensive evidence based report and were able to command confidence within and out with the organisation. The report and the briefings for the Finance Committee and Board, presented complex issues in an understandable form and the presentations were presented in a professional and assertive manner during what was a difficult time for the Trust and stakeholders. RSM made a significant contribution to the acceptance of a revised plan by both the Board and the TDA. RSM also produced a series of recommendations to improve the overall financial governance within the Trust and the finance function.

In short the work was done professionally, at pace and in a respectful but challenging way and represented great value for money. As a post script their projections turned out to be very close to the eventual outturn.

Colin Gentile, Ex Interim FD, NHS Provider Trust, now Chief Financial Officer, Kings College Hospital NHS FT
RSM UK Consulting LLP has been engaged by a number of NHS provider organisations to conduct independent financial reviews following a down turn in financial performance and/or have reported significant variances against their financial plan. If you would like to discuss any matters raised in this commentary or indeed if you have concerns within your Trust then please contact

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