

BUDGETARY PLANNING AND CONTROL

FOREWORD

- 1 The specific requirements of this SoPP are ***in addition*** to those set out in the general statements on '*Standards of Professional Practice*' on pages 1 to 4 inclusive. In particular, the attention of members is drawn to the section on *Standard of Care* at page 2.
- 2 All organisations need to manage performance so that their financial and strategic objectives are achieved and management and financial stakeholders can be confident in the associated control processes. The proper construction and control of budgets is central to this, to safeguard the organisation's viability and the effective delivery of its objectives. This requires a comprehensive financial planning and approval framework; consistent and rigorous processes for constructing budgets, both capital and revenue; sound methodologies for assessing the financial impact of proposed expenditure; compatibility with other management and performance data, and a control system that sets clear responsibilities and produces prompt and accurate monitoring information on performance against budgets.

INTRODUCTION

Applicability

- 3 This SoPP applies to all members involved in the preparation, application, monitoring and supervision of budgets and any other aspect of the budgetary process.
- 4 The public's reliance on professional accountants for the integrity of the finance function includes a dependence on financial information for:
 - 4.1 Ensuring efficient and effective use of resources.
 - 4.2 Maintaining sound internal control.
 - 4.3 Assisting in sound management decision-making.
 - 4.4 Demonstrating accountability
 - 4.5 Taking remedial action where needed.

Good budgetary planning and control is key to all these areas.

- 5 This SoPP sets standards with which Institute members are required to comply in order to ensure the integrity of the budgets for which they are responsible and to discharge their obligations to ensure appropriate standards of planning and control.
- 6 Some of the requirements of budget systems and outputs, as well as the responsibilities of the director of finance, will be determined by the legal and regulatory framework within which the organisation has to operate. Where specific professional accounting standards have been developed by recognised standard setting bodies for particular organisations, CIPFA's Ethics SoPP states that members are required also to comply with those standards.

Scope

- 7 This SoPP covers the entire process of determining the income and expenditure of the organisation for the period under consideration and the subsequent control and monitoring of actual and forecast progress against the authorised budgets.
- 8 It therefore covers multi-year capital and revenue expenditure and income budgets, including the funding of capital investment, and the planning, authorisation, implementation, recording and control of those budgets, whether responsibility is devolved or retained at the centre.
- 9 Most public-sector organisations control their financial processes by reference to annual budgets of expenditure and income, and this SoPP is framed so as to cover those processes. Some organisations may focus performance control on indicators and ratios of financial performance over rolling periods, or on a net financial position associated with production outcomes. In these circumstances, different detailed practical criteria will apply; but sound control still depends on having clear and planned objectives and metrics with which actual performance is routinely compared. The key principles set out below will still be relevant in all the appropriate areas of financial activity.
- 10 The guidance contained in this SOPP has been drawn up so as to be relevant to most sizes of organisation. Members working in small organisations will need to uphold the key principles of the SOPP but adjust their application to the circumstances in which they work.

Objectives

- 11 To support the deployment of financial, human and physical resources with maximum efficiency, security and accountability in the achievement of the organisation's aims.

KEY PRINCIPLES

Relationship of budgets to the objectives of the organisation

- 12 **Directors of finance should take all reasonable steps to ensure that budgets are planned as an integral part of the strategic and operational management of the organisation and are aligned with its structure of managerial responsibilities.**

Guidance

- 13 Budgets should be constructed to support the delivery of the organisation's strategic objectives and policies. This involves:
 - 13.1 Multi-year planning of income & expenditure, covering capital expenditure & disposal and the sources & applications of funding.
 - 13.2 Alignment of the construction and approval of the budget with policy planning.
 - 13.3 Construction of the budget analysis in such a way as to be able to identify resources against policies or other appropriate divisions of business activity. This may require more than one analysis and presentation of budget information in order to deal with issues that affect more than one organisational unit or do not match normal authorisation and management structures.

- 14 Organisations need an integrated planning and monitoring system that facilitates an assessment of progress against, and the effectiveness of, both policies and performance. This involves:
- 14.1 Mechanisms for feedback from previous and current budgets.
 - 14.2 Inclusion of results of effectiveness studies of whatever kind.
 - 14.3 Linkages to other management and performance information.

Consistency, transparency, prudence and accuracy of budgets

- 15 **Directors of finance should take all reasonable steps to ensure that budgets are constructed on the basis of reliable data of past performance and rigorous assessments of future resources and commitments, and that policies and priorities are evaluated in an open, consistent and thorough manner.**

Guidance

- 16 Robust budgets require the assessment or forecasting of the following (where applicable to the specific organisation):
- 16.1 Incoming financial resources:
 - 16.1.1 Taxes.
 - 16.1.2 Grants and subsidies.
 - 16.1.3 Sales, fees and other operating income by class of business.
 - 16.1.4 Donations.
 - 16.1.5 Partnership contributions.
 - 16.1.6 Recurrent and non-recurrent funds.
 - 16.1.7 Investment income.
 - 16.1.8 Loans.
 - 16.2 Cash flows.
 - 16.3 Expenditure commitments on:
 - 16.3.1 Staff.
 - 16.3.2 Property.
 - 16.3.3 Contracts.
 - 16.3.4 Other operating expenses.
 - 16.3.5 Financing costs.

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- 16.4 Variations to service levels arising from:
 - 16.4.1 Strategy and policy changes.
 - 16.4.2 Changes in the volume of activity.
 - 16.4.3 Demographic changes.
 - 16.4.4 Legislation and Government regulations or other externally imposed targets.
- 16.5 The impact of inflation and taxation changes on levels of income and expenditure.
- 16.6 Human and physical resources needed to support expenditure plans.
- 17 The collection, analysis and presentation of this information should be carried out within a planning framework using consistent methodologies that are approved by an appropriate senior finance manager, usually the director of finance or equivalent.
- 18 The accuracy of budgets depends on the development of appropriate processes, agreed at non-executive level, that are clearly communicated to all parties to the preparation of those budgets and that are consistently and comprehensively applied.
- 19 To be acceptable, a budget must be compiled in a way that is understood by all those involved. Determination of priorities and decisions on resource allocation normally fall to a board, council or equivalent. Those with that accountability have responsibility for the decisions and their practical consequences. The responsibility of directors of finance is to ensure, by clarity of presentation and quality of communication, that the processes and the options are well known and understood and that risks, uncertainties and the degree of accuracy are made clear, so that there is confidence in the system and choices can be made on policies and business outcomes and not technicalities. This requires :
 - 19.1 An agreed and rational system for prioritising objectives.
 - 19.2 A rigorous evaluation of alternatives using appropriate financial and management techniques which may include:
 - 19.2.1 Full life-cycle costing.
 - 19.2.2 Discounted cash flow.
 - 19.2.3 Cost/benefit analysis.
 - 19.2.4 Design and feasibility studies.
 - 19.2.5 Assessment of physical resource availability.
 - 19.2.6 Risk assessment.
 - 19.2.7 Market research.

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- 19.3 A consistent application of budget construction techniques, such as:
 - 19.3.1 Base.
 - 19.3.2 Incremental.
 - 19.3.3 Zero base.
 - 19.3.4 Activity base.
 - 19.3.5 Programme.
- 19.4 The choice as to which approach or mixture of methods to use is a matter of local discretion, but the responsibility of the director of finance is to ensure that there is a clear understanding of the reasons for the choice and the advantages and disadvantages of each of the options. Any changes to the conventions used must be explained, and existing figures re-worked to be compatible. The starting point from which budgets are considered is a crucial factor in determining future variations and equality of treatment of competing budgets. A consistent application of the chosen budgeting techniques is fundamental.
- 20 The effectiveness of budgets depends to a great extent on their relevance to the management processes of the organisation. The director of finance should take all reasonable steps to ensure that:
 - 20.1 Budget data is compatible with the accounting system of the organisation, and uses common definitions.
 - 20.2 Budget documents are compiled in a manner that facilitates comparisons with the organisation's financial statements and other financial planning and performance reports.
 - 20.3 There is compliance with internal and external regulations and limitations.
 - 20.4 Budgets are produced in a timely manner that allows for their proper scrutiny by those responsible for taking decisions.
 - 20.5 Budgets are issued in time to monitor the whole period of performance to which they refer.
- 21 A budget should safeguard an organisation's capacity to respond to unforeseen changes in circumstances and demands. To do this, the director of finance should recommend appropriate policies on:
 - 21.1 The level of general and earmarked reserves.
 - 21.2 Provisions for identifiable liabilities.
 - 21.3 Working balances.
 - 21.4 Contingency planning.
 - 21.5 Treatment of inflation, e.g. whether the budget should be cash-based or be constructed on a real-terms basis.
 - 21.6 Borrowing levels and costs.

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- 22 A budget will often contain a balance between sub-objectives or policies, such as service maintenance & development and asset maintenance & development, or between products, or between front-line services and support functions. The director of finance should take all reasonable steps to ensure that the relationship between these aspects is clearly demonstrated and understood.
- 23 Budgets should be accompanied by a clear explanatory and interpretative report, highlighting the basis of preparation and risk issues.

Effective and controlled implementation of budgets

- 24 **Directors of finance should take all reasonable steps to ensure that responsibilities for budget management and control are unambiguously allocated, that commitments are properly authorised, and that budgets are related to clear objectives and outputs.**

Guidance

- 25 To achieve an effective implementation of a budget, the director of finance should take all reasonable steps to ensure that:
- 25.1 Each part of the budget is compiled with the participation of whoever will be responsible for its control and performance
 - 25.2 The outcome of budget decisions, whether capital or revenue, are communicated to all those that need to know. Budget targets should be expressed in output terms as well as financial terms wherever possible.
 - 25.3 Responsibility for each element of the budget is delegated to a named individual. There must be no ambiguity about the responsibility for the authorisation and monitoring of any financial or non-financial element.
 - 25.4 There are clear rules for dealing with:
 - 25.4.1 Additions to budgets, including any additions for inflation.
 - 25.4.2 Virement between budget headings.
 - 25.4.3 The commitment of future years' budgets by spending decisions in the current year.
 - 25.4.4 The treatment of over- and under-spending at the year end.
 - 25.5 Appropriate systems are in place to authorise, verify and record budget commitments and actuals, including comprehensive systems of internal control.
 - 25.6 There are links to operational systems so that operational performance can be assessed alongside financial performance.
 - 25.7 Budget data is accessible to those responsible for budgets in a timely and understandable way.

Measurement and monitoring of performance against budgets and objectives

- 26 **Directors of finance should take all reasonable steps to ensure that effective systems and procedures operate to monitor progress against budgets and their objectives at regular intervals, and that appropriate reporting mechanisms are in place.**

Guidance

- 26 Monitoring of budgets is essential, not just to verify expenditure or income against targets but also to identify changing patterns or circumstances that may give rise to the need for corrective management action or changes in policy. Therefore, the director of finance should take all reasonable steps to ensure that:
- 26.1 Regular monitoring of all aspects of the budget takes place, whether it is income, expenditure, borrowing levels, project progress, operational outcomes or cash flows, and that the results of such monitoring is appropriately documented.
 - 26.2 Resources from donations, grants or partnerships are being used for the purposes for which they are intended, and that any necessary documentation is safeguarded.
 - 26.3 Monitoring data is used to predict out-turns by providing mechanisms and systems to achieve this.
 - 26.4 Monitoring results are reported upwards to the appropriate level and in an appropriate manner for the level of management or non-executive.
 - 26.5 Action is taken where results indicate that a change of policy, practice or budget is needed.
 - 26.6 Monitoring data is fed back into the planning cycle for the following years' budgets.
- 27 It is normally the responsibility of the director of finance to monitor and report on the overall financial position of the organisation at appropriate intervals and in time for corrective action to be taken.