Health & Social Care Information Centre

HSCIC Financial Management and Reporting

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Introduction

1. The HSCIC financial management function, systems and process must ensure effective management of our current expenditure of around £225m. However, we need the financial capability and capacity of a much larger organisation because we manage an additional £1bn of expenditure on behalf of the DH. The importance of financial management was recognised by the organisation when the financial management review was incorporated into the Transformation Programme.

2. The specific focus of this note is to update the Board on options for improving our financial reporting.

Current position

Financial management capability

3. To help establish the baseline position we commissioned PWC to conduct an independent Health Check of our financial management capability. This was completed in November 2013, and in summary concluded that:

   - the finance team had achieved a great deal in establishing the operational systems and processes needed to enable the HSCIC to operate and fulfil its statutory duties; but
   - we have a low level of maturity in the 'value add' activities, such as forecasting & planning, analysis and decision support, and in reporting, and
   - to achieve good to excellent levels of financial management, the organisation should establish workstreams across a number of key areas, covering: capacity and capability, structures and culture, and systems and processes.

Financial reporting

4. Our current reporting capability for HSCIC expenditure is heavily reliant on spreadsheets, which is resource intensive and increases the risk of error. The way our finance ledger is set up allows us to manage and report expenditure by our cost centre structure and by the type of expenditure (we have a reasonably detailed coding systems for staff costs, contractor costs, and other types of non-staff expenditure).

5. Financial reporting of the DH Programme expenditure that we manage is constrained by the information we are able to secure from DH systems, but since the majority of this expenditure is with third party suppliers, we are less constrained by limitations of a financial system.

6. The finance elements of the current performance pack is comprised of the following:

   - Finance KPIs for HSCIC expenditure and DH Programme expenditure, covering expenditure Vs plan, and a forecast accuracy KPI;
   - HSCIC management accounts covering in year expenditure;
   - A DH Programme expenditure report covering the variances to planned expenditure by individual programme; and
   - HSCIC Finance operational KPIs (BPPC, debt management and expenditure covered by POs).

7. Engagement across the business, discussions at the Board and feedback from the DH and our key commissioners, suggest the priorities for enhancing our financial reporting capability for both HSCIC and DH Programme expenditure are as follows:

   - Forecasting accuracy – it is difficult to draw conclusions from the expenditure against the 2013/14 plan because the planning process for this year was completed in very difficult circumstances, but it is clear that our forecasting at cost centre/Directorate level is still poor for both the HSCIC and DH Programme expenditure;
   - Service line and project reporting – there is a high level of demand for us to develop the capability to report our expenditure against our service areas and programmes;
   - Analysis and interpretation – for both the Exec team and the Board it is important to explain the causes of finance variances from business cases and plans, to understand the implications for future costs and value for money, and to have the capability to explore options for corrective action; and
   - Timeliness – business areas would ideally have real time availability of expenditure and forecasts data. Whilst the Board will typically expect the finance reports to follow a month end, the current approach requires Board meeting to be around five weeks after the end of the month.

8. The feedback from the Board on their requirements for financial reporting, and on the performance pack more generally, highlighted the alternative priorities that exist for Boards. To support the assurance function, the Board report would provide extensive and detailed information, to facilitate an extensive discussion of the management action taken by the Exec team across all areas of expenditure. An alternative approach would be for the Board to use more of the time available to focus on the specific financial risk areas identified by the Exec team, and particularly focus on options for corrective or mitigating actions.

The financial management review

9. As recommended by the PWC report we have a established the following workstreams:

   - Financial strategy
   - Policies and guidance
   - Forecasting, budgeting, reporting and business intelligence.
   - Finance capacity and capability
   - Finance for non-specialists
   - Systems and processes

10. There are severe limitations on progress towards delivering our objectives for financial reporting whilst using the current financial system, so we are planning to make a tactical investment in a new financial reporting system (in advance of the change to a new system and shared service provider in Q3 2015/16). Deriving the benefits from the new system will depend on us delivering structural, process and cultural change across the organisation, which will require a substantial amount of time and effort for the finance team and all business areas across the organisation. The finance team and many of the business areas already face resource constraints: the finance team has an average vacancy rate of approximately 25% for this year, and there are still more than 10% of the permanent posts that remain unfilled (including two posts in the Financial

Strategy, Reporting and Change team). Whilst we can make some short term significant improvements, the process we are currently planning will take around 18 months to complete.

Financial reporting issues

11. This section discusses three aspects of the financial management review that has the most direct implications for financial reporting:

- Financial system
- Service line and programme reporting
- Variance analysis

Financial system

12. The new HSCIC financial reporting system will run alongside the existing transactional system and services provided by outsource provider (NHS SBS). The system will take data directly from the ledger, and other sources such as payroll, but will also enable data input by the business areas - see Annex 1 for scope of proposed new financial reporting system.

13. The procurement process has started and the supplier will be selected in early March, with a go-live date for phase 1 in July 2014. We are planning three phases to secure all the objectives of the project, although only phase 1 has been planned in detail – see below:

Phase one (go-live July 2014):

- Streamlined cost centre reports for HSCIC cost centre managers to enable easier tracking of actuals and ability to forecast more accurately
- Increased data capture detail & standard reporting template for DH programmes
- Automatic consolidation capability of 170+ cost centre reports to facilitate production of the monthly Finance Board Pack

Phase two:

- Reporting of actuals and forecast by service line and programme (scope to be determined by strategic decisions in relation to cost allocation and time recording)
- Provision of business analytics: ad hoc reporting, KPI’s and dashboards etc. where a business need is identified
- Easier production & reporting of HSCIC Board Pack

Phase three:

- Easier production of HSCIC Financial & Statutory Reporting

14. At present it is not clear what functionality will be provided by our new shared service provider (Arvato), which we have provisionally committed to by around Q3 of 2015/16. However, the value for money case of the interim HSCIC reporting system is based on the benefits it will deliver over the next 18 months, including much of the preparatory effort that will support the transition to a new outsource supplier.

15. The key benefits of phase 1 will be to provide better control and more timely information to managers of the HSCIC business areas, and to increase the speed and accuracy of the central finance monthly close process for HSCIC expenditure. Phase 2 will deliver improvements to our analytics, and an ability to report expenditure by service line and programme.

Service line and programme reporting

16. Reporting our expenditure by service line and programmes will put us in a much better position to assess the value for money of our outputs. On the programme side, we can do the financial planning, monitoring and analysis for both DH and HSCIC expenditure for the major programmes we deliver.

17. However, many costs centres are mapped to multiple service lines and/or programmes, and all service lines and programmes are supported by expenditure spread across a number of costs centres.

18. We have a relatively large number of staff managed in centralised pools (e.g. technical IT staff, information assurance specialists, project managers and business analysts, programme finance, commercial, and programme comms staff), so a service line and programme reporting system needs a mechanism to assign the cost of these staff to the areas they are supporting.

19. The predecessor IC implemented a time recording system shortly before the merger to create the current HSCIC, but this cannot be rolled out across the new organisation in full. The platform on which the IC system is based could not accommodate the larger organisation, the coding would have to be extended to reflect the new service lines and programmes, and it would need major restructuring to reflect our current requirements.

20. The new finance system will provide a suitable platform for a time recording system, but designing and implementing the system will be a major undertaking. The first stage will be to agree a position on some critical high level issues:

- Scope. The wider the scope, the greater implementation investment and ongoing management cost. The system implemented by the predecessor IC covered all delivery areas and all staff, which has the benefit of enabling a full ‘service catalogue’, but it also increases implementation and ongoing costs. An alternative would be to start with the level 1 items on the Portfolio, with the potential to extend over time;
- Specificity. In the first instance we might expect to define the service lines based on the top level descriptor on the Portfolio database, but service areas are typically a combination of narrower services, and programmes are made up of a number of projects. Experience of the predecessor IC, and in many NHS Trusts that have introduced service line reporting, suggests that as the system is developed there is pressure from the business to define according to increasingly narrow service lines; and
- Precision. We will need to decide the level of precision we require. For example, we could include all staff in the scope or only pooled staff that spend a significant proportion of their time working across service lines and programmes, and we would structure the reporting in short time segments (e.g. 15 minutes) or use broader time segments (e.g. half days).

21. There will be a trade-off between more granular management information, and the cost and complexity of the system. The ongoing opportunity cost of time recording systems

can be substantial - for example, if all staff spent 20 minutes a week completing their time reporting, the opportunity cost of staff time will be approximately £500k per year.

22. We have not yet planned phase two of the system implementation in detail but provisionally we are aiming to have introduced service line and programme financial reporting in place by Q4 2014/15.

Variance analysis – affordability and value for money

23. We should be able to quickly analyse the causes of financial variances against budget for both HSCIC and DH Programme expenditure, explain the implications for future expenditure, and explore the options for corrective action.

24. During the current financial year, virtually all areas of the HSCIC are significantly underspending against their budget. We believe this is predominantly due to over budgeting, but even with a fully staffed finance team it would be impossible to review all areas of the business on an ongoing basis. This year we have typically provided high level analysis of HSCIC underspending at an aggregate basis only, and the reporting has been limited to the area of underspending only - i.e. most of the underspend is because we have employed less staff than expected in the budget.

25. With tighter budgets in 2014/15 we would expect few business areas to be underspending, so will have greater capacity to produce and report focussed drill down analysis where there are variances. We will aim to include the cross-over implications of variances between DH Programme and HSCIC but this will be limited by the absence of service line and programme level financial reporting.

26. For the DH Programme Expenditure, which is primarily commercial spend with third party suppliers, the financial report has typically included the reason for material underspends (e.g. delay to contract approval, reduced prices, slippage in deployments) and we have provided an indication of the implications for future costs. In addition, the Programme Delivery KPI includes a financial RAG rating alongside the other performance indicators.

27. Value for money analysis is difficult in the public sector where the benefits are typically non-financial and are often not quantified (compared to commercial organisations that target cash flow, profit and share value). It is rare for public sector organisations to routinely report an analysis of the value for money of their activity, but to achieve good practice we would report the implications for delivery performance alongside financial variances (which we are partially providing already for the areas covered by the Programme Delivery KPI).

Proposed changes for the start of 2014/15

28. Despite the limitations of our financial system we can make improvements to the financial reporting.

HSCIC reporting

29. We propose to make the following changes to the standard reports for HSCIC financial reporting:

    - Provide a simple summary table setting out the aggregate position for the HSCIC year to date and forecast outturn expenditure – see Annex 2

- Provide a breakdown of expenditure by type, with a more granular commentary against each type of expenditure – see Annex 3
- Provide a breakdown of expenditure year to date and forecast outturn by Directorate. Whilst this is a limited substitute for service line and programme financial reporting, it will be a mechanism for identifying drill down analysis of the areas with a material variance – see Annex 3.

DH Programme Expenditure

30. The financial position for the portfolio of DH funded programme expenditure is presented as an appendix to the Performance Pack for the private session of the board only, reflecting the commercial sensitivity of the figures contained in the report. The report includes current and future years expected expenditure and comparison with the known/ expected funding envelopes available for each year (both revenue and capital).

31. We are currently proposing no major changes to our routine reporting schedules for DH Programme expenditure. However, with the implementation of the IGAR report we are in discussion with the DH about future financial reporting requirements. If there is a decision to adopt a single system-wide set of reports, we will work with our partner organisations with an aim to create a single standard set of financial reports. Clearly, this could involve all stakeholders needing to compromise different organisations and Boards have different priorities and preferences

Drill down analysis

32. Major risks to the financial position and affordability issues are highlighted in the commentary in both the HSCIC reports and the DH Programme reports, but it is intended that the information provided in either or both of these will be supplemented with specific variance reports where a business area or programme has a large variance, particularly against forecast outturn.

33. The variance report will seek to answer the following questions:

- **What is the nature of the variance** – e.g. delayed expenditure, or avoided expenditure?

- **What is the cause of the variance** – e.g. approval delays, failure to recruit, commercial issues, etc?

- **What are the implications for future expenditure** – e.g. will there be an increase or decrease in overall costs, in what year will there be an expenditure impact, is there cross-over implications between DH Programme and HSCIC expenditure, if known what are the implications for future affordability?

- **What are the implications for delivery** – e.g. is the programme delayed, is there an under-delivery, has service quality suffered, will the objectives of the programme or service be met?

- **What are the options for management action** – e.g. secure additional resources or move resources from another business area, re-negotiation timetable/deliverables, etc?

34. Many of these issues should be led by the programme and/or service area, and we would expect significant risks to delivery to be reported elsewhere in the performance report, so it is proposed that the drill down reports will be produced by the business areas working with their finance business partners and/or programme accountants. In addition, whilst the variances can be identified as part of the month end process, the indepth drill down analysis will often take longer to complete than the time available between the month end process and the Board meeting. These bespoke report will typically be available in the following month.

KPIs

35. The current RAG tolerances on the Financial KPIs, which are replicated at Directorate level for management purposes, are as follows:

- **Budget v actual/forecast:** Green between 0.5% overspend and 3% underspend, Amber between 3% and 5% underspend, and Red over 5% underspend or over 0.5% overspend
- **Forecast accuracy**: Green within 2%, Amber between 2% and 4%, and Red over 4%
- **Operational finance**: timeliness of paying invoices (BPPC), outstanding debt over 90 days, and proportion of expenditure with invoices.

36. The Board has raised the issue of whether it was appropriate to assign a red RAG rating to underspending. Whilst underspending could be an indication of efficiency, it could also be an indicator of programme slippage or under-delivery. It is a useful mechanism to indicate areas for potential concern for further investigation so the proposal is that we leave this measure unchanged.

37. In addition, it has become apparent our accounting system processes makes it very difficult to achieve the forecast accuracy KPI, even though the forecast is only for one month in advance because expenditure is only certain when the invoice is received, and we have a relatively large amount of expenditure where the timing and value of invoices is difficult to predict. For example, the contractor suppliers are relatively erratic in their invoicing, which averages nearly £1m per month. However, costs are accrued/ prepaid each month as accurately as possible, although this is a manual and time-consuming process. We are exploring options for making the expenditure more predictable, and the new financial system will give budget managers greater control, so we propose to also leave this measure unchanged.

Actions required of the Board

38. The Board is asked to comment on the following:

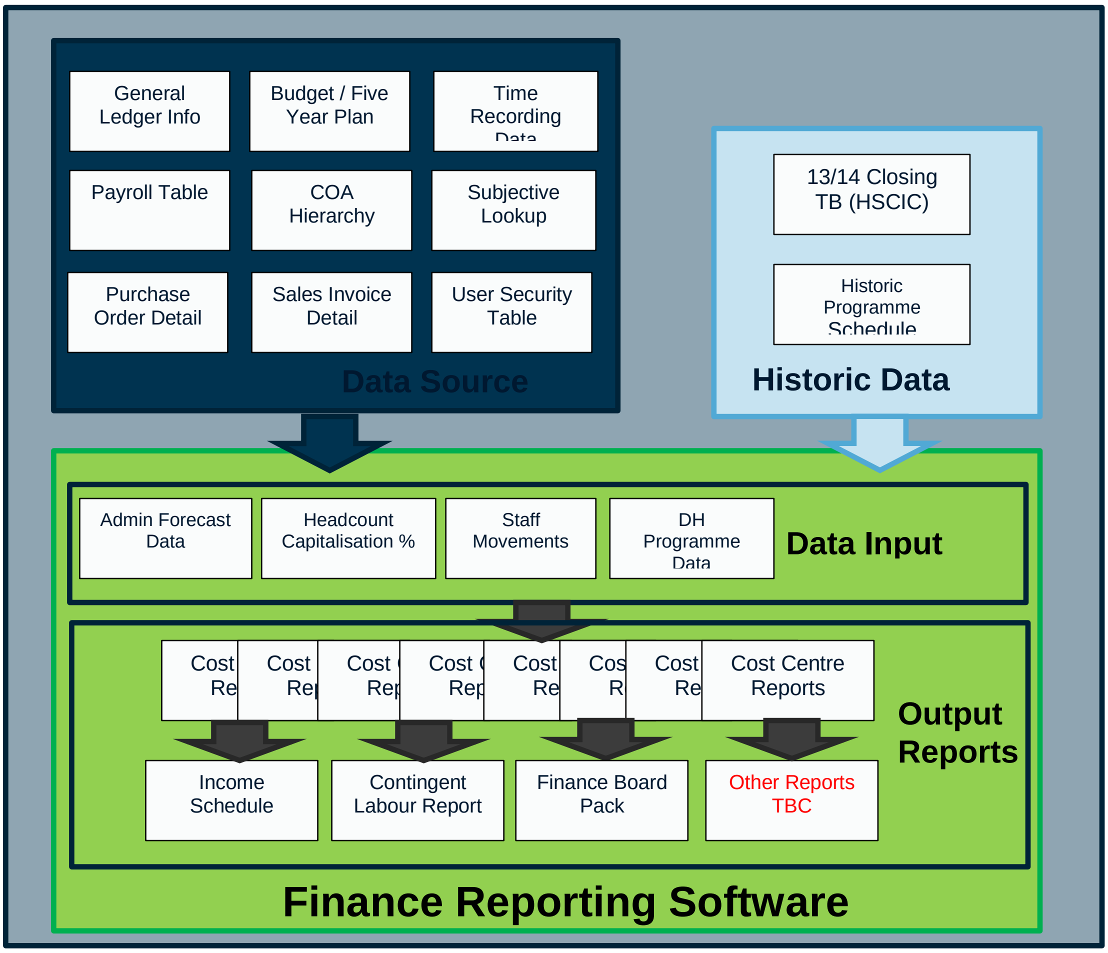
- the priorities for reporting of HSCIC expenditure and DH Programme expenditure (para 7)
- the financial reporting issues discussed: new system implementation (paras 12-15), Service line and programme reporting (paras 16-22), and variance analysis (paras 23-17)

39. The Board is asked to approve the proposals for 2014/15 financial reporting:

- HSCIC expenditure (para 29 and appendices)
- DH Programme expenditure (paras 30-31)

- The drill down analysis (paras 32-34)
- KPIs (paras 35-37)

Annex 1: Financial system scope

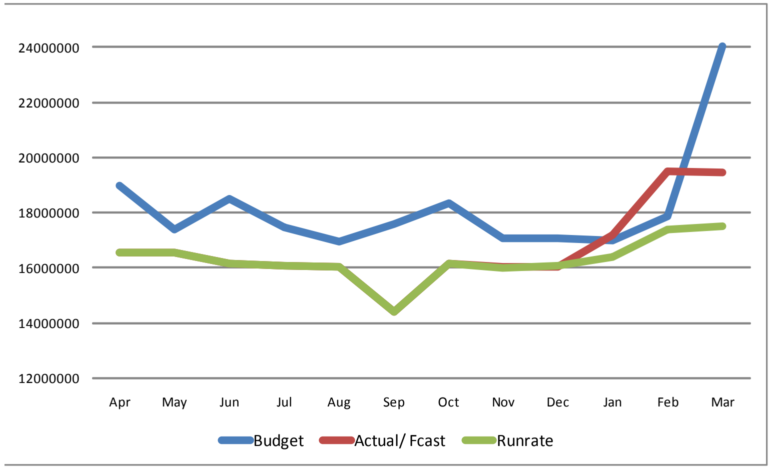


Annex 2: HSCIC Expenditure summary

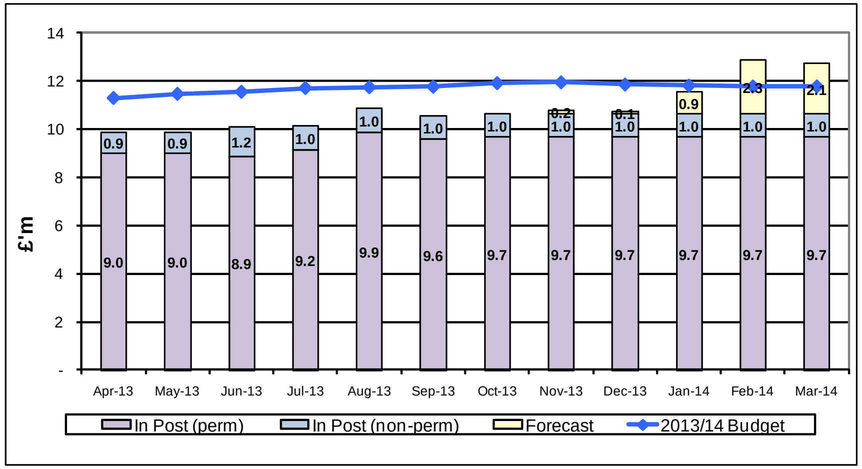
2013/14 HSCIC Management Accounts as at (month) (year) **NOTE: all figures are for illustrative purposes only** **Summary Position**

£'m	Year-to-Date			Full Year		
	Budget	Actual	Var	Budget	F'cast	Var
Total Income	(163.2)	(160.0)	3.2	(221.3)	(217.3)	4.0
Total Staff Costs	105.2	94.2	(11.1)	140.6	131.3	(9.2)
Total Other Costs	47.9	43.4	(4.5)	69.7	59.9	(9.8)
(Surplus)/ Deficit	**(10.0)**	**(22.4)**	**(12.4)**	**(11.1)**	**(26.1)**	**(15.1)**
Depreciation (ring-fenced)	8.3	6.6	1.7	11.0	9.4	1.6

The latest consolidated forecast indicates that we will end this financial year with a surplus of £15m, primarily due to under-recruitment to vacant posts. However, this forecast still contains unrealistic recruitment assumptions for the remainder of the year therefore it is expected that this may rise to £17m-£20m, which is where DH expect us to end the year.



Monthly trend of gross expenditure for the organisation for the original budget (blue), the latest forecast (red) (9 months of actual costs and 3 months of expected costs) and an extrapolation (runrate) of the position if the current staff position remained at December levels for the remainder of the year (green).



Actual and forecast staff costs, distinguishing between the current permanent (purple) and non-permanent (blue) staff costs plus the forecast increases for the remainder of the year (yellow). The blue line shows the original budget.

Annex 3: HSCIC Expenditure by type

2013/14 HSCIC Management Accounts as at (month) (year) **NOTE: all figures are for illustrative purposes only** **Detail by Income/ Expenditure Type**

£'m	Year-to-Date			Full Year		
	Budget	Actual	Var	Budget	F'cast	Var
Income						
Grant in Aid	(129.8)	(128.0)	1.8	(173.0)	(173.0)	0.0
Income	(33.5)	(32.0)	1.4	(48.3)	(44.3)	4.0
Total Income	**(163.2)**	**(160.0)**	**3.2**	**(221.3)**	**(217.3)**	**4.0**

£4m full year variance comprises:

1.1	Reduced recovery from NHS E on project A to reflect reduced costs due to delay in programme approval
3.8	Income for Project X that will not now be received from NHS England but will be covered from GiA underspend
(0.7)	Additional income from DH to cover the costs of project Y
(0.2)	Other
4.0	

£'m	Budget	Actual	Var	Budget	F'cast	Var
Staff Costs						
Permanent Staff	96.7	84.8	(11.9)	129.3	118.4	(10.9)
Non Permanent Staff	8.5	9.4	0.9	11.3	13.0	1.7
Total Staff Costs	**105.2**	**94.2**	**(11.1)**	**140.6**	**131.3**	**(9.2)**

£9m full year variance comprises:

5.5	Delayed recruitment and several leavers in Technical Architecture leading to delays in the development of Asset X for programme Y
4.5	Delayed recruitment in Commercial leading to delays in contract signing for reprocurement of A
(0.9)	Unbudgeted staff recruited for Service B in SSD; covered by additional income from NHS England
0.1	Other
9.2	

£'m	Budget	Actual	Var	Budget	F'cast	Var	Detail
Other Costs							
Professional Fees	22.3	15.4	(6.8)	29.8	22.9	(6.9)	£6.9m lower than budgeted legal fees due to early settlement of dispute with X
Information Technology	8.3	7.0	(1.3)	10.8	9.8	(1.0)	
Travel & Subsistence	4.1	3.2	(0.9)	5.4	4.6	(0.9)	
Accommodation	8.5	8.6	0.2	11.2	11.7	0.4	£0.6m additional costs incurred in location B due to unbudgeted rent increase
Marketing, Training & Ev	1.1	1.0	(0.1)	1.5	1.5	(0.0)	
Office Services	2.4	2.3	(0.1)	3.1	3.1	(0.0)	
Other	1.4	5.8	4.4	7.7	6.3	(1.4)	
Total Other Costs	**47.9**	**43.4**	**(4.5)**	**69.7**	**59.9**	**(9.8)**	

Annex 4: HSCIC Expenditure by Directorate

2013/14 HSCIC Management Accounts as at (month) (year) **NOTE: all figures are for illustrative purposes only** **Detail by Directorate**

£'m	Year-to-Date			Full Year			
	Budget	Actual	Var	Budget	F'cast	Var	
LSP Delivery							
Income	(1.2)	(1.6)	0.4	(1.6)	(2.0)	0.4	X Directorate is forecast to end the year £m under budget due to delays in recruitment on Programme A. The delay is due to a longer than anticipated approval process for PSBCs. To date this has not impactted the planned start date of the programme; however, there is a risk that any continued recruitment delays could delay the start by up to 6 months
Staff Costs	15.4	13.1	2.3	20.4	16.8	3.6	
Other Costs	2.3	0.6	1.7	3.0	1.7	1.3	
Net GiA funded	**16.5**	**12.1**	**4.4**	**21.8**	**16.5**	**5.3**	
Programmes Delivery							
Income	(1.6)	(8.0)	6.4	(6.3)	(11.9)	5.6	Y Directorate is forecast to end the year £m over budget due to the expected funding from NHS England for Programme B being withdrawn. It has been agreed that HSCIC will fund the programme for this year from overall surplus, but that this does not set a precedent for future years.
Staff Costs	11.7	12.2	(0.5)	15.6	19.0	(3.4)	
Other Costs	1.8	4.6	(2.7)	7.5	6.3	1.2	
Net GiA funded	**12.0**	**8.8**	**3.2**	**16.8**	**13.4**	**3.4**	
Operations & Technical Services							
Income	(14.0)	(9.2)	(4.8)	(18.8)	(13.3)	(5.5)	Z Directorate is forecast to end the year £m over budget due additional costs from the extension of Programme C. The programme is now expected to continue for 6 months longer than budgeted, as agreed by Portfolio Board on (date)
Staff Costs	31.3	25.5	5.8	42.0	36.3	5.7	
Other Costs	6.5	3.1	3.5	8.6	5.4	3.2	
Net GiA funded	**23.8**	**19.4**	**4.4**	**31.8**	**28.4**	**3.4**	
Data & Information Services							
Income	(16.4)	(12.7)	(3.7)	(21.3)	(16.3)	(5.0)	
Staff Costs	23.5	22.4	1.1	31.1	30.3	0.9	
Other Costs	16.9	11.8	5.1	22.3	16.7	5.6	
Net GiA funded	**24.0**	**21.5**	**2.6**	**32.2**	**30.7**	**1.5**	
Finance & Corporate Services							
Income	(0.2)	(0.9)	0.7	(0.3)	(1.0)	0.8	Directorate is £m over budget due to increased Legal Fees for the X dispute
Staff Costs	18.6	15.0	3.6	25.1	20.8	4.3	
Other Costs	21.5	19.6	1.9	27.4	25.4	2.0	
Net GiA funded	**39.9**	**33.7**	**6.2**	**52.2**	**45.2**	**7.0**	
Information Assurance	**2.8**	**2.7**	**0.1**	**4.1**	**4.4**	**(0.3)**	
HR & Transformation	**2.1**	**1.8**	**0.3**	**2.8**	**2.6**	**0.2**	
Clinical	**1.5**	**1.0**	**0.4**	**2.0**	**1.6**	**0.3**	