

**TRANSPORT FOR LONDON**

**AUDIT COMMITTEE**

**SUBJECT: BUDGETARY CONTROL**

**MEETING DATE: 23 JANUARY 2008**

---

**1 INTRODUCTION**

- 1.1 As part of its on-going work to review the effectiveness of internal control in place throughout TfL the Committee has asked for a paper on the budgetary control arrangements within the organisation to be presented annually as a standing item. This paper is updated where appropriate from that presented to the Committee last year.

**2 CONTROL OF EXPENDITURE**

- 2.1 Planned and actual expenditure is controlled via a number of processes to ensure that TfL is able to carry out its statutory functions in the most economic, efficient and effective manner. They are designed so as to provide a balance between effective control and necessary flexibility to ensure managers can effectively deliver the functions for which they are accountable.

- 2.2 These processes can most easily be described in the following 3 headings:

- Business Planning and Budgeting
- In-year Financial control
- Procurement Authority

These control processes and the supporting system of monitoring and reporting are described in the remainder of this paper.

In some cases there will be minor changes to the levels of authority if the proposed revisions to Standing Orders detailed elsewhere in this agenda are approved at the next Board meeting.

**3 BUSINESS PLANNING AND BUDGETING**

- 3.1 The business planning and budgeting process is the mechanism whereby resources are allocated to priorities on a short to medium term basis. The most recent Plan revisited last year's business plan

remaining focused over the length of the current funding settlement (5 years to 2009/10). Next year's plan will be based on the recent settlement received from Government as part of the Spending Review 2007 (SR07) which covers the period to 2017/18. Whilst financial expenditure will be modelled over the whole of this long period, it has not yet been decided what time frame the published plan will cover.

- 3.2 The process commences in the Spring when key planning assumptions are distributed across the group, along with indicative financial targets, to allow modes and directorates to commence their bottom-up planning. During the process there are a number of workshops with finance and planning staff across the organisation, MDs, the Board and key stakeholders to ensure the plan reflects agreed priorities, but also that recurring income exceeds recurring costs and that the plan is robust and deliverable, able to withstand scrutiny particularly by the rating agencies.
- 3.3 The resulting Business Plan, approved by the Board each October, outlines the direction and scope of the organisation's activities along with the related outputs and outcomes that are achievable within the resources available. Importantly, it will ensure there is financial balance over the settlement period. A version of the Plan is submitted to the GLA to be consolidated as part of the Mayor's budget and presented to the London Assembly in January and February.
- 3.4 The Business Plan itself is made up of an operating plan and an Investment Programme, a distinction that is important in that they are controlled differently. The first year of the Business Plan forms the basis of an operating and capital budget which is approved by the Board in the March preceding the financial year to which it relates. This Budget is likely to differ from that set out in the first year of the Plan owing to the impacts of:
  - The changes in the forecasts during the second half of the preceding year as the Plan is usually based on the second quarter forecast (the six periods ending in mid September) and much can change between then and the following March when the budget is approved
  - The effects of any changes agreed with the Mayor following the final agreement of his overall Budget by the London Assembly in mid February
  - Any errors or omissions that may have been discovered subsequent to October that particularly affect the budget year
  - Any new issues that may have emerged in the second half of the year that would impact the budget year
- 3.5 The Budget consists of a set of balanced financial statements which are supported by schedules of headcount in terms of Full Time Equivalents (FTEs) as well as deliverables and Key Performance

Indicators (KPIs) to enable proper monitoring of the resultant outputs and outcomes. Once agreed by the Board, the Budget is distributed to each business within the SAP financial system. Each of the Managing Directors is thereby given their financial authority and people resources within which to manage their business for the coming year.

- 3.6 A subset of KPIs and deliverables is selected for each business unit to form the senior management scorecard. Performance against this scorecard forms one part of the senior management bonus award (in conjunction with personal performance and values & behaviours), paid annually to all managers in paybands 4 and above.

#### **4 IN-YEAR FINANCIAL CONTROL**

- 4.1 Following approval of the Budget and associated deliverables, responsibility for delivery is held by each Managing Director, who in turn delegates to cost centre and project managers within their directorates to manage the agreed and approved budgets and initiate and approve individual purchase requisitions and payments as is appropriate.
- 4.2 In respect of both the operating and capital budgets all business units are required to reforecast every quarter (i.e at periods 3, 6, and 9) so that the latest understanding of the likely outturn for the year can properly reflect the activities that each area believes is necessary to meet their proposed outputs and outcomes whilst meeting any new circumstances that have arisen or will arise. Each period, they are also required to amend forecasts for any significant events.
- 4.3 This is then reviewed by the modal Finance Director or equivalent with their executive committees, both to approve the forecast and to ensure there is an understanding of what their business to date has or has not achieved compared with their operational targets.
- 4.4 All these forecasts are input into the SAP financial system, KPIs into the Executive Reporting system and for physical deliverables and outcomes into Activity and Project Reporting (APR) system. This enables a Group position to be prepared and reported upon as well allowing business units to look at what each other is doing.
- 4.5 The forecast is across the whole lifecycle for projects and at least for 2 financial years (ie the current year and the one after) for recurring expenditure, with the focus being on the current financial year. This is to ensure that whilst attention is paid to the immediate financial and delivery performance of the organisation, the impact of that performance on the future year is also identifiable. This then forms a natural lead into the annual business planning process.
- 4.6 In respect of the Capital Budget there is also a requirement for projects to be reviewed, particularly in regard to the business case and affordability, by the appropriate body at appropriate stages in the

project lifecycle before expenditure is authorised and can be incurred. For projects making cumulative commitments up to £5m budgeted and £1m unbudgeted each business unit has its own approval body:

- The Funding Gateway Meeting (FGM) for LUL
- The Surface Approvals Board (SAB) for Surface
- The London Rail Executive Group (LREG) and DLR Board for London Rail Business Unit and
- The Corporate Investment Review Group (CIRG) for all central departments.

4.7 For projects between £5m and £25m (budgeted) or unbudgeted expenditures between £1m and £10m, approval is escalated from the relevant body as described above to the Managing Director, Finance, via the Project Review Group (PRG). This process is currently under review with the intention of formalising a 'gateway review process', ensuring that the approval process is aligned to these key decision points in the lifecycle of projects, and which formally focuses on project business cases, financial affordability and deliverability risks.

4.8 Each period, a review is performed of the extent to which projects are still within their approved funding authority. Where projects are approaching their authority limit, project managers are asked to submit a supplementary authority paper including a business case to the relevant review body and ensure expenditure forecasts across the project programmes remain within funding constraints.

4.9 Budgeted projects between £25m and £100m or unbudgeted expenditure between £10m and £25m are authorised by the Commissioner following review by the Project Review Group and those over £100m (budgeted) and £25m (unbudgeted) by the Board, except for emergencies when the Commissioner can authorise but then report to the Board. This is in accordance with Standing Orders.

## **5 PROCUREMENT AUTHORITY**

5.1 Once financial authority (and funding authority in respect of projects) has been granted, the budget holder may sanction expenditure as described above in paragraph 4.1. This does not automatically confer on the budget holder procurement authority which is required to be able commit to contracts etc. unless such authority was specifically part of the request.

5.2 Procurement authority is an additional control designed to enable contacts and other commercial agreements to be scrutinised by those with the necessary experience or professional expertise to assess the contractual implications for TfL. For straightforward low value purchases, procurement authority is delegated widely; correspondingly, procurement authority for complex and/ or high value transactions is vested in very few individuals.

- 5.3 Procurement authority may only be exercised by those individuals who have been delegated such authority within each business unit, and may only be applied up to the limit set for their given role. The procurement element of the SAP system provides the mechanism for regulating the application of procurement authority.
- 5.4 Each Chief Officer may grant procurement authority for up to £25m. Subject to the relevant Chief Officer's written consent, their senior officers and respective Heads of Procurement may approve up to £5m, while officers below the level of senior officer may approve up to £500k.
- 5.5 Transactions above £25m up to £100m are approved by the Commissioner or in his/her absence the Managing Director of Finance. Where the Commissioner judges that the transaction is exceptional in nature he/ she may choose to refer it to the Finance Committee and then the Board for approval. All transactions exceeding £100m require Board approval.

## **6 MONITORING AND REPORTING**

### **Each Period**

- 6.1 Control of expenditure is managed at the lowest level by cost centre managers for recurring activities, and by project managers for non-recurring pieces of work. Cost centre managers have available to them a suite of automatic reports, generated once a period (every 4 weeks), available on-line direct from the SAP system to inform them of the financial and staffing performance for their cost centre. Project managers review the performance of their project periodically through a variety of project management systems, and are scrutinised through Programme Management Offices (PMOs) within each mode.
- 6.2 This performance is then aggregated, such that each period the Managing Director of each business unit produces a report setting out both the financial and operational performance within the period, and associated risks and issues. In order to review this performance information, there are ten times a year a Business Management Review (BMR) of each business unit and an Investment Management Review (IMR) with each of business units with large Investment Programmes (LUL, Surface, London Rail and the Major Project Unit within the corporate directorates). These are two stage processes:
- Group Business Planning and Performance (for the overall business performance and financial situation) and Oversight (for projects and programmes) carry out detailed analysis and discussions with each mode and directorate of their BMR/IMR reports to fully understand progress during the period and year to date along with the impacts on the business for the year as a whole. This culminates with a briefing to the Commissioner by the Chief Finance Officer and the Head of Oversight on issues

arising from the reports, and any items for inclusion within the agenda for the meeting. The BMR reports are made available to senior managers to ensure maximum visibility activities across TfL and to facilitate joined up working.

- Any major issues that are likely to be high profile in the public domain or impact the business strategically will be raised at the BMR/IMR itself so that full discussion can be had between the relevant MD (with their senior management team) and the Commissioner. Otherwise the BMR/IMR allows the Commissioner to be involved in decision making on strategic issues. In respect of the IMR there are discussions on Independent Engineer's reports on key projects or programmes as they arise, giving assurance that major issues have or have not been considered and outlining the way forward that has been agreed with the project team.

6.3 In addition, each period Group Business Performance produces a period 'Barometer' for the Commissioner (copies of which are also sent to the Chief Officers) which is a report outlining the trends on the key operational key performance indicators and the overall financial position against budget. The Oversight Team issues a modal IMR briefing note to the Commissioner, copied to the modal PMO highlighting any issues arising with the delivery of key projects.

### **Quarterly**

- 6.3.1 There is a review of cross-cutting items in respect of the Investment Programme Delivery with all MDs at the quarterly Investment Programme Chief Officers Meeting (IPCOM).
- 6.3.2 Based on the BMR/IMR reports, the Chief Finance Officer submits an Operational and Financial report and an Investment Programme report to the Finance Committee for review before it is then submitted to the TfL Board. The appropriate modal period BMR reports the basis of the Managing Directors' performance reports to the Advisory Panels.
- 6.3.3 Externally, following review by the Board, a synopsis of the Board report is submitted to the GLA for inclusion in the Functional Bodies' Quarterly Budget & Performance Monitoring Report to the London Assembly. This often forms the basis of questions from the Assembly Budget Committee, and wider questions put to the Mayor as part of his regular question process. In addition, the LUL quarterly report is submitted to DfT officials who review the key movements/issues with representatives from LUL and TfL.
- 6.3.4 A summary of key monitoring and reporting arrangements is attached as **Appendix 1**.

## **7 SUMMARY**

- 7.1 The above outlines an exhaustive process of control and review of TfL's activity as the year progresses so as, where possible, to avoid any surprises and ensure mitigating actions are put in place, if necessary, to correct adverse trends and to ensure financial discipline remains sound. This whole process is further entrenched with TfL's requirement to ensure that the Rating Agencies continue to uphold TfL's AA rating status. Timely delivery and financial rectitude are key to maintaining this status.

## **8 RECOMMENDATION**

- 8.1 The Committee are asked to note TfL's detailed budgetary control and review processes.

# TfL's performance reporting framework

