

TRANSPORT FOR LONDON

AUDIT COMMITTEE

SUBJECT: BUDGETARY CONTROL

DATE: 7 MARCH 2012

1 PURPOSE AND DECISION REQUIRED

- 1.1 As part of its ongoing work to review the effectiveness of internal control throughout TfL, the Committee receives a paper on the budgetary control arrangements within the organisation, presented annually as a standing item. This paper is updated where appropriate from that presented to the Committee last year.
- 1.2 The Committee is asked to note the paper.

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 four headings:
 - (a) Business planning and budgeting;
 - (b) In-year financial control;
 - (c) Project authority (stage gate approval); and
 - (d) Procurement authority.
- 2.3 These control processes and the supporting system of monitoring and reporting are described in the remainder of this paper.

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 (usually the time period covered by TfL's funding agreement with Government.) The last two years have seen a change to the 'traditional' business planning cycle, due to the timing of the Government Comprehensive Spending Review that took place in 2010. A new Business Plan was produced in March 2011 that spanned the length of the new settlement received from Government to 2014/15. This was then updated in a 'light-touch' way for progress on key deliverables and the latest financial forecast in December 2011.

- 3.2 During 2012, TfL will revert to a more 'traditional' cycle, whereby the key strategic assumptions for the Business Plan are reviewed in the first half of the year, before a detailed financial plan is settled during the summer for publication of the overall Business Plan in the Autumn/Winter.
- 3.3 However, with a Mayoral Election and the Games during the summer, the process will be built to ensure it can appropriately plan for and take into account the new Mayoralty, and allow the maximum amount of 'back-office' staff to support operational colleagues during the Games period.
- 3.4 During the year, on an internal basis, the quarterly forecast process will continue to be used to confirm ongoing key planning assumptions and the financial position. Over the last year this has included regular meetings with Operating Business Finance Directors to ensure a better two way flow of information and understanding.
- 3.5 The Budget consists of a set of financially-balanced statements. This is supported by schedules of headcount in terms of Full Time Equivalents (FTEs) as well as milestones and Key Performance Indicators (KPIs) to enable proper monitoring of the resultant outputs and outcomes. Once agreed by the Board, the Budget is confirmed to each business within the 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 milestones is selected for each business unit to form the senior management scorecard. Performance against this scorecard forms a key component of the senior management bonus award (in conjunction with TfL's overall performance, personal performance, values and behaviours), paid annually to all managers in pay bands 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. They, in turn, delegate through Directors to cost centre and project managers within their business units 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). This means 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 while 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 These forecasts are then reviewed by the Finance Directors of the operating businesses or with their respective business Boards and by the Managing Directors in the corporate support functions, both to approve the financial impacts and ensure they can be funded, 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 inputted into the SAP financial system, and for milestones in respect of investment projects, into the ProSight system, so that each period a Group position can be consolidated and reported upon.
- 4.5 The forecast is across the whole lifecycle of projects and for recurring expenditure for the period of the Business Plan, with the focus being on the current financial year. This is to ensure that while attention is paid to the immediate financial and delivery performance of the organisation, the impact of that performance on future years is also identifiable. In addition, modelling and capture of data within SAP is carried out each quarter through the forecast process. This creates a base financial plan for 10 years ahead (currently through to 2020/21), within a framework of assumptions on grant funding, borrowing, etc. This then forms a natural lead into the annual business planning and budgeting process.
- 4.6 The forecast process includes reviews and monitoring of efficiency savings which are included within the budgets and continuously aspires to achieve more than target.

5 PROJECT AUTHORITY

- 5.1 The Business Plan itself is made up of an operating plan and a capital plan/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. In respect of the capital budget (and discrete projects/programmes in the operating budget), there is also a requirement for projects to be reviewed at relevant stages in the project life cycle. This review is carried out particularly in regard to the business case and affordability, by the appropriate body before expenditure is authorised. Each business unit has its own approval body for projects with expected final cost of up to £5m budgeted and £2m if unbudgeted.
- 5.2 Projects with a total value greater than £2m (unbudgeted) or £5m (budgeted) require authorisation by the Managing Director, Finance, who sits on the appropriate business unit Board. Projects above these values (£2m unbudgeted or £5m budgeted) are reviewed through the Corporate Gate Approval Process, which provides assurances that a project or programme is :
 - (a) Deliverable – it is likely to deliver the expected benefits within the declared cost/time/performance envelope;
 - (b) Affordable – the level of expenditure and financial risk involved is acceptable in light of TfL’s overall financial position when set against other priorities; and
 - (c) Value for money – it provides the optimum combination of whole-life cost and quality (or fitness for purpose) to meet users’ requirements.
- 5.3 Corporate Gates normally apply to a project at the following stages of their project lifecycles:
 - (a) Gate A – Project commencement;
 - (b) Gate B – Single option selection;

- (c) Gate C – Pre-tender;
- (d) Gate D – Contract award;
- (e) Gate E – Project close; and
- (f) Gate P – Programme review for annualised programmes of minor schemes.

- 5.4 Each period a review is performed to confirm projects are still within their approved funding authority. If there is a likelihood of exceeding that authority, when appropriate a supplementary or next stage authority paper including a business case, is submitted to the relevant review body to ensure expenditure and commitments do not exceed the authorised amount.
- 5.5 Budgeted projects between £25m and £50m, or unbudgeted projects between £10m and £50m, are authorised by the Commissioner. Those between £50m and £100m (budgeted and unbudgeted) are approved by the Finance and Policy Committee, while those over £100m (budgeted and 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.
- 5.6 The Independent Investment Programme Advisory Group (IIPAG) was established in May 2010 by TfL. IIPAG provides independent assurance and expert advice to the Mayor of London concerning TfL's Investment Programme as published from time to time, including all maintenance, renewals, upgrades and major projects. The IIPAG will consider issues of economy, efficiency and value for money in preparing its advice. IIPAG's reviews are normally applied to projects of £50m or greater, or for high risk projects.
- 5.7 IIPAG will also conduct systemic reviews of project methodology, best practice and governance, and present findings and recommendations to the Commissioner and Chief Officers. Agreed action plans are recorded and tracked through meetings between the TfL Leadership team and IIPAG.
- 5.8 Quarterly dashboards reporting progress against plan, budget and deliverables are published for all major TfL Projects and Programmes, and considered at Finance and Policy Committee.

6 PROCUREMENT AUTHORITY

- 6.1 Once Budgets are approved and financial authority 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.
- 6.2 Procurement authority is an additional control designed to enable contracts and other commercial agreements to be scrutinised by those with the necessary experience or 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.
- 6.3 Procurement authority may only be exercised by those individuals who have been delegated such authority within each operational 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.

- 6.4 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.
- 6.5 Transactions above £25m up to £100m will be approved by the Commissioner or in his/her absence the Managing Director, Finance. Where the Commissioner judges that the transaction is exceptional in nature he/she may choose to refer it to the Finance and Policy Committee and then the Board for approval. All transactions exceeding £100m require Board approval.

7 MONITORING AND REPORTING

- 7.1 Following Horizon, Group Business Planning and Performance (GBP&P) coordinate with finance colleagues across TfL to produce financial information reports. These reports are normally submitted to the Finance Leadership Team (FLT) and then onto the Leadership Team (LT).
- 7.2 The Finance Leadership Team has a bigger reviewing role as well as directing the finance function on key pan-TfL financial direction. For example, the Consolidated Financial Summary (CFS) is reviewed by the FLT before circulation to the LT. The FLT meets fortnightly and is composed of the MD Finance, the Chief Finance Officer, Finance Directors, Group Treasurer and Head of Finance Business Support Function.

Each Period

- 7.3 Control of expenditure is ultimately managed by cost centre managers for recurring activities, and by project managers for non-recurring pieces of work within the scope of their delegated budgets or authorities. Cost centre managers have available to them a suite of automatic reports, generated once a period (every four 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 the Programme Management Office (PMO).
- 7.4 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 compared to budget, and associated risks and issues. In order to review these periodic reports, the Commissioner holds ten times a year a Business Management Review (BMR) of each business unit. A recent change is that the MD, Finance will be responsible for the Corporate directorates' BMRs and the Commissioner will be responsible for the Operating Businesses. Each BMR involves a two stage process:
- (a) A review by GBP&P and the Chief Finance Officer of each area's BMR report. This culminates with a briefing to the Commissioner by the Chief Finance Officer.
 - (b) 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 itself so that full discussion

can be had between the relevant Managing Director (with their senior management team) and the Commissioner/MD Finance. Otherwise, the BMR allows the Commissioner to be involved in decision-making on strategic issues.

- 7.5 Crossrail performance is reviewed through the separate Sponsor Board arrangements; however, each period a Crossrail BMR is held focusing on delivery and coordination issues. Crossrail expenditure is also reported in the consolidated financial summary (see below) and in the quarterly Operational and Financial report (OFR).
- 7.6 Each period a periodic Consolidated Financial Summary (CFS) and a TfL Business Performance Report (BPR) are produced. The CFS goes to the Finance Leadership Team meeting and then on to the Leadership Team meeting. The BPR is sent to the Finance Leadership Team and Leadership Team. The CFS reports income and expenditure compared to budget and the latest forecast. The BPR reports performance of operational key performance indicators from the Budget and TfL Scorecard as well as Investment milestones.
- 7.7 Each quarter, a meeting is held with the operational units, GBP&P and Customer Experience to discuss patronage demand for London Underground, Buses and London Rail to identify any key trends and to agree underlying assumptions for forecast demand. A report on patronage and fares revenue is prepared by GBP&P (the Passenger Demand Summary report), in coordination with the virtual teams and circulated to the Finance and Policy Committee.
- 7.8 In addition, a regular report on savings delivery progress has been produced and reviewed at the Efficiency Delivery Board (EDB). In future, this will take place at the new Efficiencies, Savings, Transformation and Revenues (ESTR) meeting on a quarterly basis, building upon efficiency work carried out in each individual business area.

Quarterly

- 7.9 Based on the BMR reports, the Chief Finance Officer submits an Operational and Financial report and an Investment Programme report to the TfL Board (normally this will go to the Finance and Policy Committee first). A report on projects authorised by the Commissioner, MD Finance and Tube Lines Board is prepared and circulated to the Finance and Policy Committee.
- 7.10 The latest BMR reports form the basis of the Managing Directors' performance report to the quarterly Advisory Panels relating to each of the operating businesses: Rail and Underground and Surface Transport.
- 7.11 Externally, following review by the Board, the OFR is submitted to the GLA for inclusion in the Functional Bodies' Quarterly Budget and Performance Monitoring Report to the London Assembly. Specifically, they are considered at the Assembly's Budget Monitoring Sub-Committee, where the Chief Finance Officer is scrutinised on their content. This also often forms the basis of wider questions put to the Mayor as part of his regular question process.

8 SUMMARY

- 8.1 This paper outlines an exhaustive process of control and review of TfL's activity as the year progresses, and 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 rating status. Timely delivery and financial rectitude are key to maintaining this status.

9 RECOMMENDATION

- 9.1 The Committee is asked to NOTE the paper.

10 CONTACT

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