

Committee	Date:
Efficiency and Performance Sub Committee	26 May 2015
Subject: Apportionment of Costs: Town Clerk's Department, City Procurement and Information Technology	Public
Report of: The Chamberlain	For Information

Summary

This report addresses the outstanding reference to review the bases for apportioning the costs of the Town Clerk's Department, City Procurement and the IT Division. It is concerned with 'how' the City accounts for the costs of these services. Questions on 'why' we provide the services, the method of delivery and the quantum are being examined through the pressures imposed by the Service Based Review. In my own department, a number of financial services have already been market assessed or tested e.g. outsourcing of the IT function to Agilisys, internal audit benchmarking, and the insourcing of rates and council tax collection. A further detailed benchmarking task, using soft market testing, is being carried out for other aspects of the Finance function.

The revised methodologies for apportioning the costs of the three services are outlined in the main report and, in aggregate, the redistributive impacts at Fund level are as follows.

Fund	Original Basis %	Revised Basis %	Change Increase/ (Decrease)	
			%	£'000*
City Fund	60.0	61.0	1.7	201
City's Cash	36.5	33.8	(7.4)	(528)
Bridge House Estates	3.5	5.2	48.6	327
Total	100.0	100.0	0.0	0

* The 2014/15 total cost of the Town Clerk's Dept., City Procurement and the IT Division is £19.5m

Whilst the financial effect is relatively small in the context of the overall size of the funds, the redistributive impact at Committee Level is more significant as set out in the main report at Chart 2. For most Chief Officers of front line services, the changes should not be an issue as they are not responsible for the delivery of support services and neither is their performance linked to them. However for ring-fenced accounts, such as Police, the apportioned costs are a direct charge against available resources and should be subject to scrutiny by the Chief Officers concerned.

The apportionment of support service costs (or overheads) is designed to share the costs across all the activities of the organisation on a reasonable basis. However such a technique is a fairly blunt instrument and the limitations need to be recognised. For example, the apportioned costs do not represent what may be saved if a front line service were allowed to opt out of the support services provided

by the City Corporation, and neither are they necessarily an appropriate basis for charging third parties.

The City currently accounts for central support service costs in accordance with CIPFA's Service Reporting Code of Practice (SeRCOP). For local authorities SeRCOP has statutory force and establishes proper practice to ensure consistent financial reporting. However, with regard to the City's non-local authority funds, there is no requirement to follow SeRCOP.

The City could, for internal reporting purposes, take a decision that wherever possible the costs of support services will not be included with front line services but, instead, be treated as a 'one-line' management and administration cost. However, this would not avoid the task of preparing and accounting for such overheads as, on the local authority side, they will still be required for the financial statements, the budget, Government returns, CIPFA returns, etc. The main reason for non-inclusion for internal reporting purposes would seem to be that central support costs are not within the control of front line services. This is not a sufficiently compelling reason to justify the operation of two parallel accounting systems.

Recommendations

Members are requested to:

- note the methodologies being used to apportion the costs of the Town Clerk's Department, City Procurement, and the Information Technology Division together with the redistributive impacts;
- agree that the costs of central support services should continue to be apportioned to all funds and services in accordance with the local authority requirements set out in SeRCOP; and
- note the soft market testing task being undertaken for aspects of the Finance function.

Main Report

Background

1. Last September I reported on the various bases used to apportion the costs of central support services across the City Corporation's various activities. That report identified three support services, the Town Clerk's Department, the City Procurement Team and the Information Technology Division where the appropriateness of the distributions required review and updating. The Efficiency and Performance Sub-Committee resolved that for these services, revised methodologies for recovery of costs be reported back to the Sub Committee within six months, to improve the appropriateness of distributions.
2. This report addresses the outstanding reference which is concerned with 'how' the City accounts for the costs of these services. Questions on 'why' we provide the services, the method of delivery, the quantum and general value for money are being examined through the pressures imposed by the Service Based Review in order to achieve the significant budget reductions required. These pressures are visited on the local and central risk budgets (which are then apportioned as support services) of central departments in the same way as for front line

services. The reductions agreed for the Chamberlain and the Town Clerk are £2.8m and £2.0m respectively representing some 15% and 14% of each department's overall budget.

3. As part of the ongoing requirement to improve value for money, of which the SBR is a significant but not the only element, a number of services in my own department have been market assessed or tested, e.g. outsourcing of the IT function to Agilisys, internal audit benchmarking, and the insourcing of rates and council tax collection. A further detailed benchmarking task, using soft market testing, is being carried out for other aspects of the Finance function. However as Members are aware, for a number of the City's financial services, the breadth and complexity of the organisation makes benchmarking less straightforward than a simple comparison with other local authorities and these factors are being reflected in the approach and timescales for the task.
4. This report also recaps on why it is necessary to apportion the costs of central support services.

Town Clerk's Department

5. The 2014/15 cost for the Town Clerk's Department within Guildhall Administration is some £7.9m and it was previously apportioned on the basis of estimated time spent. Although the apportionments were reviewed annually for new services and restructures the underlying percentages were dated. It was also recognised that the apportionment method would benefit from greater granularity.
6. The £7.9m relates to 15 separate cost centres. As a first step in reviewing the methodology, each cost centre was considered against service definitions set out in SeRCOP and classified as either support service functions accounted for as overheads on direct services or as Corporate and Democratic Core (CDC) activities accounted for as services in their own right. A brief definition of CDC is set out at the end of appendix 1. This review changed the apportionment between CDC and support services from 56% and 44% respectively to, coincidentally, 44% and 56% (see appendix 1 chart 5) – the reduction in CDC being some £0.9m.
7. CDC services covers functions primarily provided by the Policy and Democratic Services section of the Town Clerk's Department. The costs, some £3.5m under the revised methodology, are shared between the City's three main Funds with no requirement for further apportionment. The methodology used to apportion CDC costs between the Funds is based on the number and length of Committee meetings as recorded by the Town Clerk's Department. For committees with a more corporate role and for service committees where activities span funds (e.g. the Markets Committee oversees services in City's Cash and City Fund) a further basis of apportionment, the level of turnover, was used as a proxy for the amount of business by Fund.
8. Under the revised methodology the cost of the support services element of the Town Clerk's Department is some £4.4m. Support services provided comprise human resources related costs (e.g. Corporate HR, HR Business Units, Occupational Health, Health and Safety, Training) and the Contact Centre.
9. The revised methodology apportions the costs as follows.

Service Area	Apportionment Basis
HR Business Units	£1.5m (34%) of cost. Apportioned to departments served by the Units based on employee headcount.
Occupational Health	£0.3m (7%) of cost. Apportioned to all departments except Police (both Officers and Staff) based on employee headcount ¹ .
All other HR related areas	£2.0m (45%) of total cost. Apportioned to all departments based on employee headcount ¹ excluding Police Officers.
Contact Centre	£0.6m (14%) of cost. Apportioned to departments based on records of service calls

¹. For Barbican Centre and Guildhall School, both of which have large numbers of casual staff, full time equivalents were used instead of headcounts.

10. Appendix 1 compares the impact of the change in methodology at Fund level and Committee within Fund level.
11. The new apportionment bases for distributing the support service elements of the Town Clerk's Department to Committees use data already gathered for other purposes and it should therefore be relatively straightforward to update on an annual basis. The Committee data used to apportion the CDC element between funds is not routinely recorded and was compiled manually. The Town Clerk's Department propose refreshing the Committee data annually for new/ceased committees and carrying out a complete update every three years.

City Procurement

12. City Procurement within the Chamberlain's Department is a relatively new support service, only fully formed during 2014/15 following the early termination of the contract with Accenture. Originally, apportionments were based on budgets transferred from departments at the inception of the service. However, this was mainly related to invoice processing and did not reflect the sourcing work undertaken by the team.
13. The cost of the team in 2014/15 was some £2.4m divided into three main areas; accounts payable, transactional buying and category management.
14. The revised methodology apportions costs as summarised below.

Service Area	Apportionment Basis
Accounts Payable	£1.1m (46%) of cost. Apportioned pro rata to number of invoices processed.
Transactional Buying	£0.4m (16%) of cost. Apportioned pro rata to purchase orders raised.
Category Management	£0.9m (38%) of cost. Apportioned pro rata to Officers' assessment of time spent based on annual sourcing plan.

15. Appendix 2 compares the impact of the change in methodology at Fund level and Committee within Fund level.

Information Technology Division

16. Under the Shared Services Review, the IT Division within Chamberlain's Department has undergone a major transformation process over the last three years. To support the changes in service delivery resulting from the review, Phase 1 of the transformation process involved the unification of services and budgets centrally. Prior to this phase, a significant proportion of I.T. budgets, approximately 50%, had been devolved to departments under a system of trading accounts. However, the aim of encouraging economy and efficiency through competition proved unrealistic against the objectives of integration, standardisation, continuity and security. Trading accounts therefore ceased on 31 March 2012.

17. Phases 2 and 3 of the transformation process covered the restructuring of the IT Division to refocus on improved delivery and a sourcing review, to procure from the market improved 'best in class' IT services whilst providing efficiencies and reduced costs respectively. Phases 2 and 3 were completed during 2013/14.

18. Whilst the transformation process was underway the existing methodology used to apportion the costs of the Division, some £9.2m in 2014/15, continued to be used, with the previously "traded" element being treated as a support service charge.

19. The £9.2m relates to 12 separate cost centres. In consultation with the IT Division each of the cost centres were reviewed to assess the extent to which City departments were covered by the services or systems provided. As a result four main groupings or service areas were identified. The groupings and the revised bases of apportionment are set out below.

Service Area	Apportionment Basis
Systems or services only used by specific departments	£0.2m (2%) of cost. Allocated in full to specific departments.
Corporate systems	£1.0m (11%) of cost. Apportioned to all departments pro rata to full time equivalent (f.t.e.) employee numbers.
Services available to all departments but used to a lesser extent by the institutional departments e.g. client services and project management.	£2.3m (25%) of cost. Initially apportioned 10% and 90% between institutional departments (Police, Barbican Centre, Schools) and other departments respectively. F.t.e. numbers were then used to apportion costs to individual departments.
Services related to the non-institutional departments e.g. application support and development, Agilisys managed contract.	£5.7m (62%) of cost. Apportioned to non-institutional departments pro rata to full time f.t.e. employee numbers.

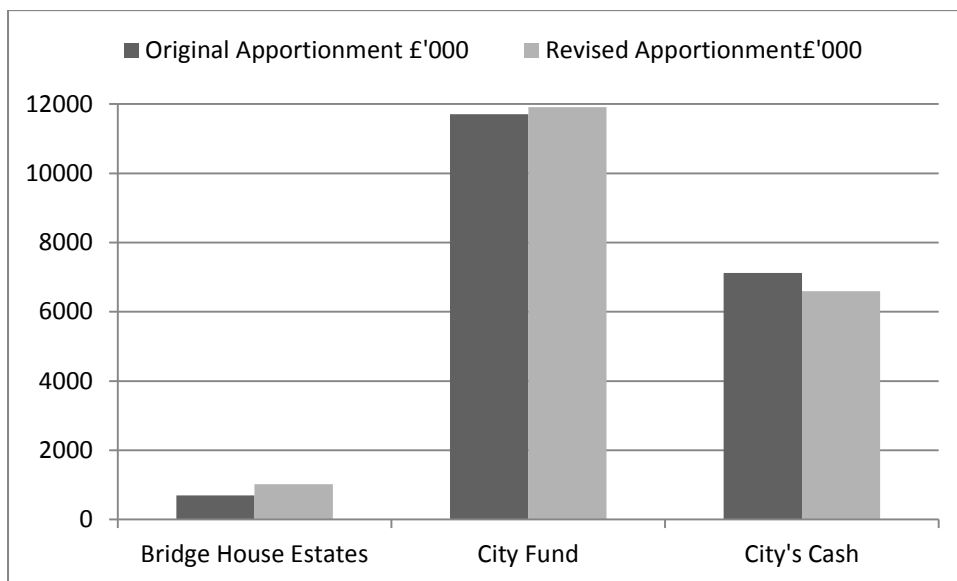
20. In arriving at the apportionment bases set out above an adjustment was made to the f.t.e. employee numbers to abate them by 50% for those departments, such as Open Spaces, where a significant number of employees do not have access to IT services.

21. Appendix 3 compares the impact of the change in methodology at Fund level and Committee within Fund level.

Implications of Review

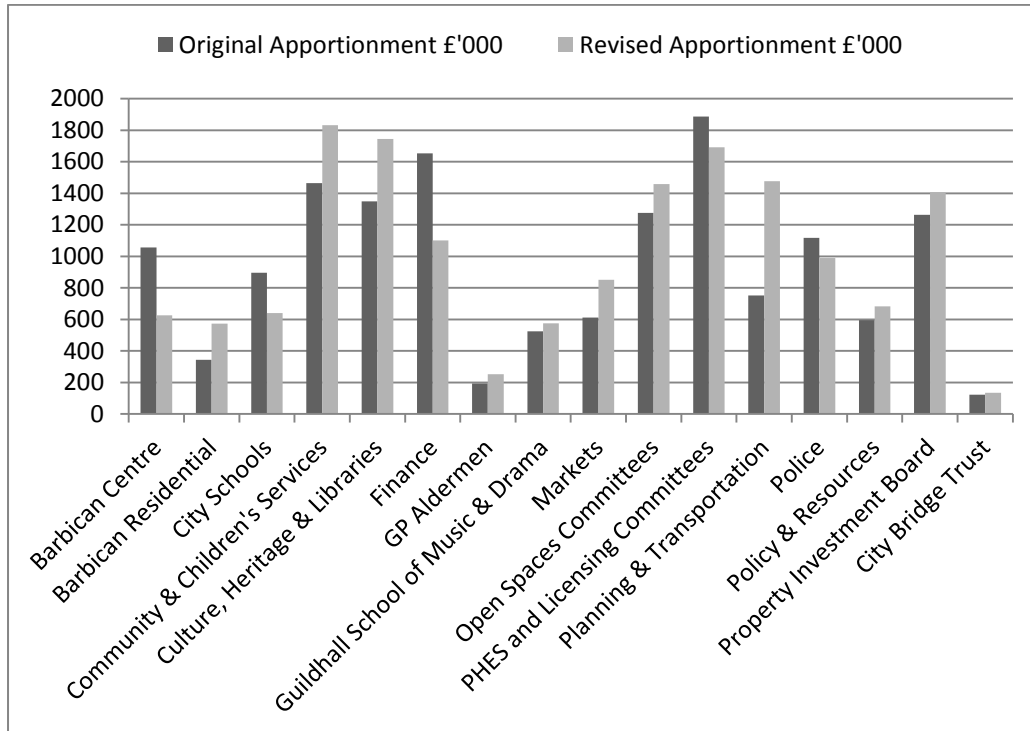
22. At Fund level, the overall re-distributional impact of the revised methodologies for the three services is relatively minor as shown in chart 1.

Chart 1: Fund Level



23. However, at Committee level the re-distributional impact is more significant as shown in chart 2 overleaf. The chart excludes the CDC reduction of £0.9m (from £4.4m to £3.5m) referred to in paragraph 6 as it would distort the table.

Chart 2: Committee Level



24. The new methodologies for the Town Clerk's Department and City Procurement were completed in sufficient time for use in the 2014/15 accounts and the new methodology for the IT Division will be used from 2015/16 when budgets are updated in the autumn/winter.
25. The "driver" for the current accounting arrangements for overheads, including support services provided centrally, is CIPFA's Service Reporting Code of Practice (SeRCOP). For local authorities SeRCOP has statutory force and establishes a definition of total cost to provide a consistent basis for all external financial reporting and statutory financial disclosures. When reporting service costs, each service must include an appropriate share of all overheads to arrive at its total cost. This definition includes costs over which service managers have no control as decisions over which costs managers should control are based on local management and delegation arrangements not accounting requirements.
26. For the City, the changes arising from this review should not be an issue for most Chief Officers of front line services as they are not responsible for the delivery of support services and neither is their performance linked to them. However for ring-fenced accounts, such as Police, the costs are a direct charge against available resources and should be subject to scrutiny by the Chief Officers concerned.
27. The apportionment of support service costs (or overheads) is designed to share the costs across all the activities of the organisation on a reasonable basis. However such a technique is a fairly blunt instrument and the limitations need to be recognised. For example:
 - The apportioned costs do not represent what may be saved by the City Corporation if a front line service were allowed to opt out of the support

services provided. Such savings would be the marginal costs and these would be determined by the nature of each item (i.e. whether it is relatively variable or fixed) and the impact on workload volumes (i.e. stepped overheads). In addition alternative suppliers may not offer the same degree of resilience/support which will impact on long term rather than short term costs.

- Neither are apportioned overheads necessarily an appropriate basis for charging third parties. A more refined analysis is likely to be required in relation to the specific service being provided.

28. SeRCOP also recognises that although the total cost requirement must be followed for financial reporting purposes it may not be appropriate for management accounting and decision making purposes. For example, local authorities, for management accounting purposes, may exclude from budget holders' reports any overheads for which they are not responsible. Whilst the City does not wholly follow this approach, Chief Officers' performance is only measured in relation to their local and central risk budgets not on the costs of apportioned central support services.

29. With regard to the City's non-local authority funds, there is no requirement to follow SeRCOP. A single line for management and administration could be included within City's Cash and/or Bridge House Estate rather than the costs being apportioned to individual services. However, our accounting practices have normally been dictated by the requirements for our largest fund (City Fund) which have then been applied consistently.

30. The City could, for internal reporting purposes, take a decision that wherever possible the costs of support services will not be included with front line services but, instead, be treated as a 'one-line' management and administration cost. However, this would not avoid the task of preparing and accounting for such overheads as, on the local authority side, they will still be required for the financial statements, the budget, Government returns, CIPFA returns, etc. Neither could the task be undertaken for City Fund in isolation as it is only when the use of resources is reviewed as a whole that the relativities of what is apportioned to each element can be considered in context and sense checked.

31. The main reason for non-inclusion for internal reporting purposes would seem to be because central support costs are not within the control of front line services. This is not a sufficiently compelling reason to justify the operation of two parallel accounting systems.

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