



14 October 2011
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A Picture of Public Services 2011

The key financial challenges facing Welsh public services



A Picture of Public Services 2011

I have prepared this report for presentation to the National Assembly under the Government of Wales Acts 1998 and 2006.

The Wales Audit Office study team that assisted me in preparing this report comprised Mark Jeffs and Emma Giles, under the direction of Simon Edge.

Huw Vaughan Thomas
Auditor General for Wales
Wales Audit Office
24 Cathedral Road
Cardiff
CF11 9LJ

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**Report presented by the Auditor General to the
National Assembly on 14 October 2011**



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Foreword



The first *Picture of Public Services* Report, published in March 2010, estimated the financial challenges facing public services in Wales and key lessons from the work undertaken by my staff and contractors. The purpose of this second *Picture of Public Services* report is to provide greater clarity on the current position and support public services in responding to the financial challenges. I intend this report to be a useful source of information for political and administrative leaders as they further develop their plans for managing with less. I also intend that the report should help the public and those involved in scrutinising public services by providing insight on the key financial and delivery issues and identifying the areas to challenge public service leaders on whether they are doing enough.

In March 2010, the exact scale of funding reductions was uncertain. We used the plans of the previous UK Government to estimate that there would be real-terms reductions of around £500 million year-on-year to devolved public spending, and that the budget in 2013-14 would be around £1.5 billion less than in 2010-11. That estimate turned out to be accurate, with a real-terms cut of £1.6 billion between 2010-11 and 2013-14. These sustained real-terms cuts are unprecedented in modern times, and most of those leading and working in public services today will never have had to deal with financial challenges of this nature.

This second national study on the Picture of Public Services sets out my perspective on the readiness of public services to manage with less. In responding to the financial constraints, public services must balance ambition and realism. Public services must be ambitious in finding new ways of delivering services, so that they can sustain and protect outcomes for lower cost. Transformation through innovation, sharing and acting on good practice and improving efficiency is the sustainable solution in the long term. But we cannot afford to ignore the short-term pressures. Transforming the way services are provided and getting public services to collaborate more takes time and a lot of effort. Public services can certainly ramp up the pace of transformation and will need to do so. But it is unlikely that widespread transformation will happen quickly enough to enable public services to bridge the funding gaps that they face in the short term. It seems likely that some form of cuts – to jobs and service levels – may be required. The challenge is to get those decisions right and to mitigate the impact on service users and wider social outcomes.



Public-service leaders will be tested in the next few years. They will need to drive through wide-ranging change that leads to more efficient and effective services. They will need to keep staff engaged at a time when they may be feeling their jobs are under threat and seeing their pay frozen. Politicians locally and nationally are already making some tough choices about which services and programmes are a priority and those which are not. Changing the form and shape of public services is often controversial with staff and the public alike. Closing down local facilities or services can be unpopular, even where doing so ultimately helps to improve the quality of services. Leaders will need to engage the public as much as possible in debates about the future shape of local services, and explain the rationale for the changes.

Public services are already taking action to reduce costs. Given that staff costs account for the bulk of public services' spending, it is no surprise that these costs have been a starting place. There have been pay freezes, recruitment freezes, and voluntary redundancies. Such action will help to bridge the funding gaps. But such action carries real risks that need to be managed. It is a cliché, but the people who work for public services are the main asset as well as the main cost. Staff will need to be at the forefront of public-service reform if changes are to be sustainable. It will take excellent leadership to get staff to go the extra mile to improve services at a time when they are being asked to take the pain of real-terms wage decreases. Effective workforce planning will be needed to make sure that organisations do not have skills gaps that impact on service quality as a result of voluntary redundancies and recruitment freezes.

It is important to state that the funding climate does not necessarily mean that services cannot or should not still aspire to improve. Indeed, the sense of urgency that budget cuts generate can be a major driver of improvement. Through transforming services and developing a culture of improvement it is possible to deliver better services and outcomes with less.

All in all, this report is challenging to public services. I make no apologies for that because getting the response right matters to the many people who rely on public services for support and to improve their wellbeing. But amongst the analysis of the difficulties they face, there are elements that provide some grounds for optimism. The need for transformation is now widely accepted and progress can be speeded up in order to put public services on a sustainable footing for the longer term. There are some exciting projects and programmes to support transformation through innovation and efficiency and a clearer vision for delivery is emerging. The biggest challenge is to cut costs sufficiently sensibly to get through the difficult next couple of years while mitigating the impact on service, service users and public service staff morale, and retaining a focus on the goal of transforming public services for the future.

Huw Vaughan Thomas

Auditor General for Wales

Summary

- 1 The scale of the real-terms funding cuts is largely as set out in our first *Picture of Public Services* report, with a real-terms reduction of £1.6 billion in devolved funding. Following a process of priority setting, the Welsh Government chose to spread the real terms cuts across all of the devolved spending areas although some areas face larger cuts than others. The Welsh Government has prioritised spending on 'frontline' areas, with its own 'back-office' spending facing the largest reductions. Devolution means there are different policy choices and priorities and there are now some clear differences in spending plans between the different parts of the UK. In particular, the NHS in Wales faces the toughest financial settlement of any of the countries of the UK. On the other hand, local government – which includes social services and education spending – has seen lower reductions to its funding from central government than in other parts of the UK.
- 2 As well as real-terms cuts, public services face rising demand. There are potential increases in demand as a direct result of the economic climate although these are uncertain. PriceWaterhouseCoopers has estimated as much as a 50,000 reduction in public and private sector jobs in Wales as a result of budget cuts. It is likely that some of those who lose their jobs will need support from the various parts of the Welsh public service. Also, non-devolved services like the police face significant cuts. The impact for those devolved public services that work with the police to deliver community safety is as yet unclear.
- 3 The NHS faces the challenge of managing real-terms spending reductions at a time when the demand for services is rising, particularly due to demographic and lifestyle factors. The track record of the NHS in resisting rising cost pressures – due to a mixture of factors including inflation, demand, and new treatments – is not good and 2010-11 was no exception, with the NHS needing around £110 million of extra funding. Its goal of reconfiguring services to lower-cost models, particularly shifting the balance of care away from hospitals to community settings, is sound. But despite some positive progress and areas of good practice, widespread reconfiguration is still in the planning stage and is unlikely to enable the NHS to bridge its funding gaps in the short term. Given the track record of the NHS and the scale of the funding gaps it faces, its goal of sustaining levels of services and jobs while reducing costs seems highly ambitious. We are concerned that it may need to review that goal if it is to avoid requiring another significant cash injection from the Welsh Government. With other Welsh Government budgets stretched, the scope to find extra money for the NHS may be much more limited than in the past.
- 4 Councils also face a significant reduction in funding. Like the NHS they also face rising demand, particularly for social services for older people and vulnerable children. Unlike the NHS, councils have been able to partially bridge their funding gaps by increasing council tax, and they also have the option of drawing on reserves if their savings plans



prove too ambitious. A series of reviews have recommended major changes to significantly increase the pace and scale of collaboration between councils. While transformation to more collaborative models may save money in the medium to long term, uncertainty about the costs, benefits and risks, and practical difficulties in making collaboration work, make it unlikely to deliver the short-term savings needed. Our work over the year shows that councils are being realistic and know they may need to reduce some levels of service and cut staff costs. Nonetheless, many need to better manage the impact of cutting costs and staff on services, service users and wider outcomes. Many need to better link their financial and service planning to clear priorities, to get workforce planning right, and to have clearer measures of the value and impact they are getting from spending on services.

- 5 The Welsh Government is taking steps to reduce its own internal costs. It is reporting savings through its internal savings programme, reducing the number of people it directly employs and plans to make significant cuts to administration and support budgets. As well as reducing its own costs, the Welsh Government faces challenges in squeezing value from the money it passes on to other organisations. Some of our work shows that the relationships between the Welsh Government and the organisations that deliver services, particularly councils, are not sufficiently clear, which can hamper effective delivery. With the First Minister demanding a heightened focus on delivery the Welsh Government will need to work hard on making these relationships clearer and more effective. This does not mean a one-size-fits-all approach. In some cases the Welsh Government may need to be directive, in others it may need to take a more hands-off supportive role. The critical challenge is to be

clear from the outset and to have an ongoing relationship that enables the Welsh Government and its partners to learn and adapt to what is actually happening on the ground.

- 6 There has been promising work to provide a national framework for developing the approach to reducing costs and improving services through efficiency and innovation. The pan-public-sector Efficiency and Innovation Programme had successfully brought together public sector leaders to develop projects across a whole range of areas. Many of those projects provide a framework for transformation: ways to redesign systems, services and parts of services to be more focused on the people that use them at the same time as cutting out waste. They also point to ways of working together to reduce the transactional costs of purchasing goods and services and owning and maintaining land and buildings. If the wider public service actually takes up the approaches being advocated, then there is real scope to improve services and cut costs. However, the cautionary note is that many of the savings are only likely to be secured in the medium to long term as they will require significant change. The Welsh Government has decided to end the Efficiency and Innovation Programme, but much of the work will be taken forwards through a new Public Services Leadership Group.
- 7 While there has rightly been a focus on transforming public services, there has been little national or collaborative direction in terms of making cuts to levels of service and jobs. While it is true that individual organisations are separately accountable, there are practical reasons why a more collaborative approach is needed. In particular, cuts to one part of the public service can, and often do, have knock-on

effects for another. The obvious example is cuts in social care, which potentially just re-direct service users and costs over to the NHS. In our view, there is a real strategic gap in terms of guidance and direction around cuts. To mitigate the impacts of such cuts, public services can plan collaboratively to take account of local and national priorities, the impact on service users and wider outcomes and any unintended consequences for other public services. Also, they can work together to keep track of what happens, and adapt to any unforeseen consequences. We hope that our *Cost Reduction Guide*, which we are publishing alongside this report, will help public services in making these tough choices.

Recommendations to support a pan-public-sector response

- a The Welsh Government is replacing the pan-public-sector Efficiency and Innovation Programme, with a new Public Service Leadership Group. The Efficiency and Innovation Programme had succeeded in bringing together public-sector leaders to identify and take ownership of various approaches to cutting costs and improving services. In developing the work of the Public Services Leadership Group, **the Welsh Government should build on this commitment to ensure that it continues to fully involve all parts of the Welsh public service and key stakeholders.**
- b Transformation is the sustainable response to funding cuts. All public services need to continue to find ways of changing the way services are provided so that they can improve quality and outcomes at lower cost. To this end, **public services should look to the work that had been done by the Efficiency and Innovation Programme, particularly work on new service models and business transformation, as a source of practical methods for improving services. In particular:**
 - i The Efficiency and Innovation Programme has developed a national programme of work on business improvement techniques like lean/systems thinking. These approaches are being increasingly adopted across public services. Currently, many public services depend on support from external consultancies. **In developing the work of the Public Services Leadership Group, the Welsh Government should**



examine options to develop the capacity and skills within the public sector in business improvement techniques, building on the work done to date, including the findings of the Lean Enterprise Research Centre (LERC) review jointly commissioned by the Wales Audit Office and the Efficiency and Innovation Programme.

ii Public services need to get better at learning from each other, and actually changing as a result. Such transfer of knowledge and practice would enable more widespread benefits to be secured from the work on New Models of Service Delivery. **The Welsh Government should work with other public services to develop a clear national framework for identifying and exchanging good practice. There also needs to be a commitment from public services to actually change, through adopting or adapting new ways of working, and a framework for supporting organisations as they go through the process of change and experimentation.**

c Public services also need to take up opportunities to make transactional savings, particularly through better procurement and better management of land and buildings. **All public services in Wales should support and engage with the promising approaches developed through the Efficiency and Innovation Programme, that now fall within the new Public Services Leadership Group.**

d The short-term financial challenges are such that some public services may need to consider reducing the level or quality of some services. **Public services across Wales should work together in planning cuts, and in monitoring and mitigating the impacts on service users, wider outcomes and other public services.**

Part 1 – Welsh public services face change and tough choices as a result of budget cuts and other pressures over the next four years

Following the UK Spending Review, Welsh public services face real-terms funding cuts, with large cuts in capital spending

1.1 The total amount of money available to the Welsh Government is worked out using the Barnett formula. The Barnett formula means that the Welsh Government's overall spending increases or decreases relative to public spending in England on policy areas that have been devolved. For example, if the UK Government chooses to increase spending on the NHS in England, the Welsh Government will get a proportionate increase in its total budget. Although the Welsh Government's total funding is linked to spending in England, there is no requirement to follow the same spending patterns as England. The Welsh Government chooses its own priorities and how much of its budget it wishes to spend in each area.

1.2 Following the May 2010 election, the UK Government carried out a Spending Review, which was finalised in October 2010. The Spending Review had the goal of eliminating the UK's structural deficit¹ over a five-year period. In order to achieve this goal, the UK Government intends to cut spending on public

services and welfare across the lifetime of the Parliament. The Institute for Fiscal Studies (IFS) highlights that cuts of this nature have not been seen in the UK since at least the 1950s². Public services face real-terms cuts every year for five years; since 1950 spending in services has never been cut in real terms for more than two years consecutively.

1.3 The analysis in this part of the report examines the impact on the budgets of Welsh public services in 'real terms'³. 'Real terms' means that the figures are adjusted to account for the impact of inflation. Where we use unadjusted 'cash-terms' figures, we will say this explicitly in the relevant section. The real-terms figures in this report differ slightly from those in the Welsh Government's draft budget because we have used different deflator figures to take account of inflation.

Devolved public funding in Wales will fall in real terms, with particularly large cuts to capital funding

1.4 The Welsh Government will see a real-terms reduction of 12.4 per cent in the funding available from the Treasury, using the Welsh Government's baseline⁴ (Figure 1). This reduction includes a nine per cent reduction in revenue funding over that period, and a 40.2 per cent reduction in capital funding (Figure 2).

¹ *The Financial Times* defines structural deficit as: a budget deficit that results from a fundamental imbalance in government receipts and expenditures, as opposed to one based on one-off or short-term factors.

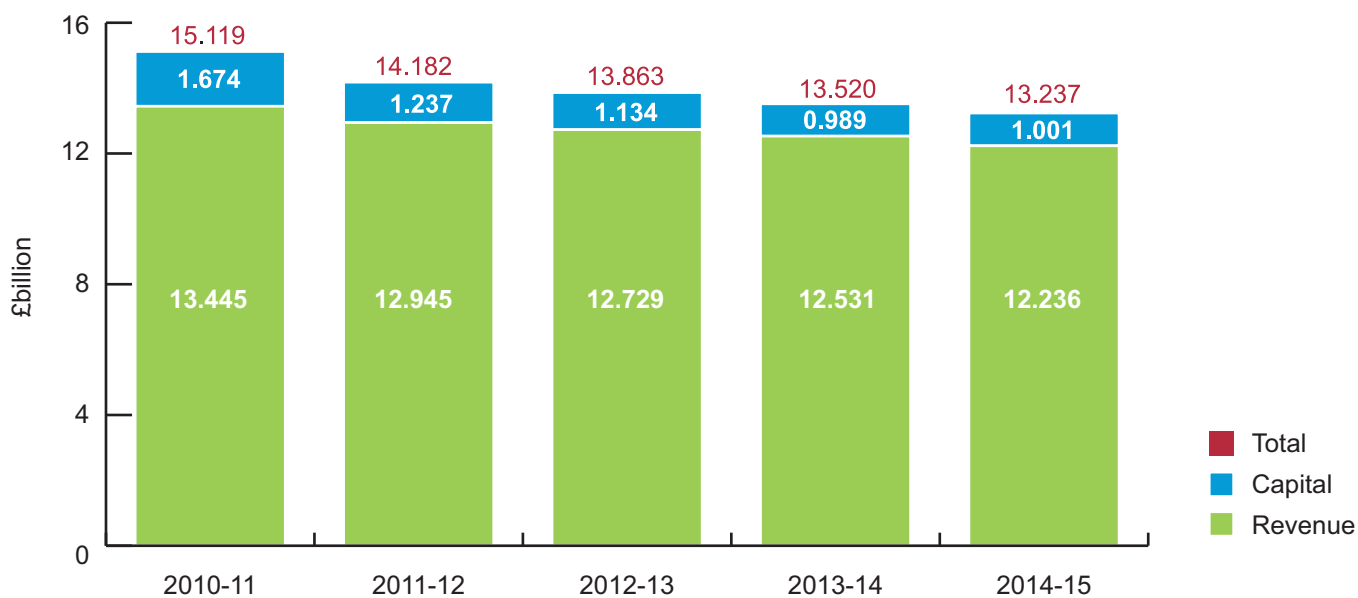
² Paul Johnson, Director IFS, *The Coming Age of Austerity*, presentation to the CIPFA 2011 conference.

³ Note on real-terms calculations: to work out the real-terms impact, we have used the Treasury GDP Deflator series. For this report, we have used the deflators issued in November 2010, as these were in place around the time when final budgets were set. The deflators have been updated since to reflect higher inflation forecasts for 2011-12 and 2012-13.

⁴ The Welsh Government uses a slightly different 2010-11 baseline from the Treasury's £15.0 billion baseline. The main difference relates to the treatment of the in-year cut as a result of the UK Government's July 2010 Emergency Budget as well as other technical factors.

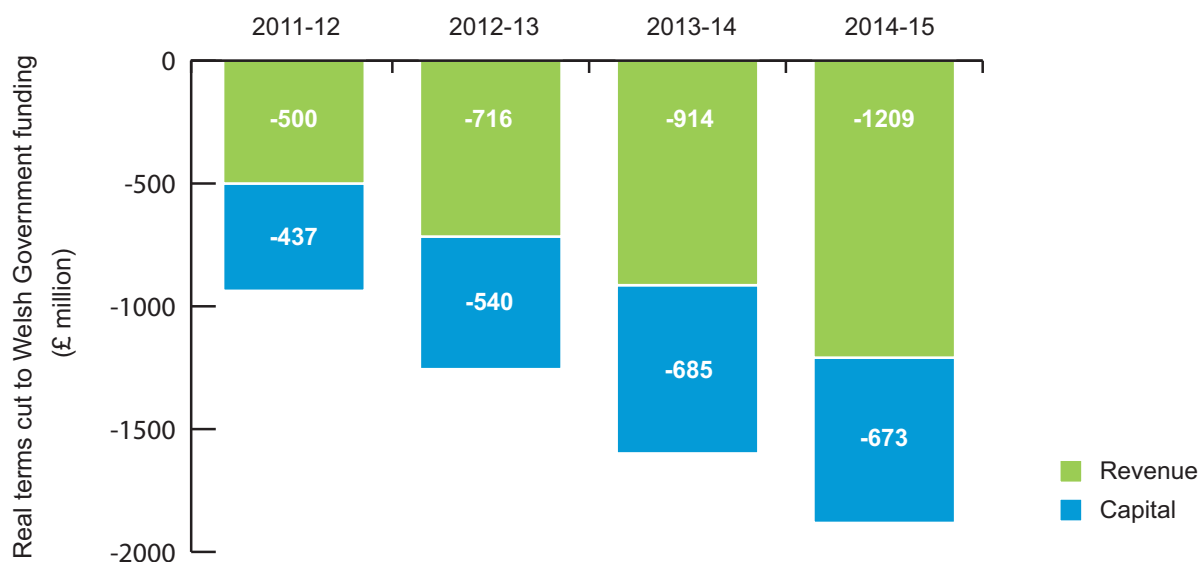


Figure 1 – Welsh Government funding in real terms (£ billion)



Source: Wales Audit Office's analysis of Welsh Government figures.

Figure 2 – Real-terms 'cut' using 2010-11 as a baseline (£ million)



Source: Wales Audit Office's analysis of Welsh Government figures.

1.5 Capital funding covers spending on infrastructure like new schools, hospitals and roads, as well as some of the major economic and regeneration projects. The sharp reduction in capital spending means public services will need to re-prioritise projects and ensure that projects stay within budget. There are also knock-on consequences, with public-sector capital spending supporting jobs in the construction and associated industries. The reduction in capital has an impact on revenue funding. Some of the ways public

services intend to reduce revenue costs, such as delivering more council services online, and treating more NHS patients in the community, will require new infrastructure to support those new practices. The Welsh Government is currently unable to borrow to increase the capital available to it, although it is seeking to gain such powers.⁵ Some potential alternative sources of investment funding are set out in **Figure 3**, some of which would have consequences in terms of increasing revenue spending.

Figure 3 – Potential sources of funding for investing in infrastructure

Local Asset Backed Vehicles are a form of partnership between the public and private sector. The public sector provides assets – land and buildings – for development. The private partner provides the finance for developing the assets into a commercial offering. It is intended to be a mutually beneficial arrangement, with the council getting the regeneration benefits for the area as well as a share of the income, and also increasing the value of the assets. The private partner benefits through its share of income from the development.

Non Profit Distributing (NPD) is a form of Public Private Partnership (PPP). It is the preferred PPP model of the Scottish Government, which has announced £2.5 billion worth of schemes using NPD. Like a Private Finance Initiative, a private company provides the up-front costs for construction and maintenance. It recovers those costs through a long-term contract with the public sector. Under NPD there is a limit on the profits that the private partner can make, and any surplus is returned to the public sector.

Prudential Borrowing enables councils to borrow money to fund investment. As with any form of borrowing, the key consideration is that the council is able to repay the borrowing. Examples of the use of prudential borrowing in Wales include borrowing to fund council home improvements, to help meet national standards. The borrowing is repaid through increases to rents (although there are strict rules around how far rents can be raised). There are examples of prudential borrowing to support service change around the UK including borrowing to fund back-office transformation and customer contact centres. The borrowing is to be paid back through savings as a result of the transformation. Prudential borrowing on an invest-to-save basis requires very robust business cases and appraisal to verify that the savings will be sufficient to repay the borrowing.

Tax Increment Financing (TIF) has been proposed by the Coalition Government to extend councils' borrowing powers, although it has not yet introduced the necessary legislation. TIF potentially allows councils to borrow money to fund regeneration projects, based on the additional future tax income from the business rates that the scheme will bring. Getting it right in practice would require councils to robustly assess the viability of projects, so that they do realise the business rate increases they need to pay back the loan. Councils will also need to be careful to ensure that the business their projects generate is truly additional. New projects that just attract businesses to move from one council area to another would mean increasing one area's tax base at the expense of the other's.

⁵ The Welsh Government has inherited the former Welsh Development Agency's powers to borrow, but any borrowing would result in an equivalent reduction in the block grant from the Treasury, meaning there would be no net gain.



The Welsh Government has cut funding for every department in real terms, but has prioritised spending on public-facing services with sharp cuts to its support services

1.6 The Welsh Government's budget showed that it intends to prioritise public-facing services.

Following a process of setting budget priorities, in its Final Budget published in February 2011, the Welsh Government decided to reduce spending, in real terms, in every department. Figure 4 shows that the two departments that received most protection were Children, Education, Lifelong Learning, and Skills and Health and Social Services. Central Services and the Public Services and Administration budgets will reduce the most sharply.

Figure 4 – Real-terms cuts to Departmental revenue budgets, compared to 2010-11

	2011-12 % Cut £ Cut	2012-13 (indicative) % Cut £ Cut	2013-14 (indicative) % Cut £ Cut
Central administration	-11.3% -£40 million	-16.1% -£56 million	-22.0% -£77 million
Public Services and Performance	-6.9% -£3 million	-12.3% -£6 million	-18.6% -£9 million
Environment, Sustainability and Housing	-4.6% -£17 million	-8.1% -£31 million	-10.1% -£39 million
Rural Affairs	-4.4% -£6 million	-8.0% -£10 million	-10.0% -£13 million
Economy and Transport	-13.7% -£82 million	-6.7% -£40 million	-8.7% -£52 million
Social Justice and Local Government	-4.1% -£180 million	-6.1% -£271 million	-7.5% -£332 million
Heritage	-0.7% -£1 million	-4.5% -£6 million	-6.7% -£9 million
Health and social services	-2.1% -£126 million	-4.3% -£252 million	-6.6% -£386 million
Children, Education, Life-long Learning and Skills	-1.5% -£25 million	-3.4% -£58 million	-4.7% -£79 million

Source: Wales Audit Office's analysis of Welsh Government budgets.

Notes

- (i) The baseline for 2010-11 is taken from the 'baseline' used in the Welsh Government's draft budget produced in November 2010. All other years are taken from the Final Budget 2011-12, published in February 2011.
- (ii) Figure shows the cumulative change from the 2010-11 'baseline'. So, for example, the Heritage Budget is expected to be 6.7 per cent (£9 million) less in 2013-14 than 2010-11, in real terms.
- (iii) The large cut in the budget for Economy and Transport in 2011-12 is largely due to a £60 million reduction in 'non-cash' on the trunk road network.
- (iv) Figures for 2012-13 and 2013-14 are indicative. The Welsh Government has put forward draft budget proposals which, if approved, would impact on the figures for 2012-13 and 2013-14.
- (v) The real terms figures differ from those in the Welsh Government's November 2010 draft budget because we have used a more recent set of deflators.

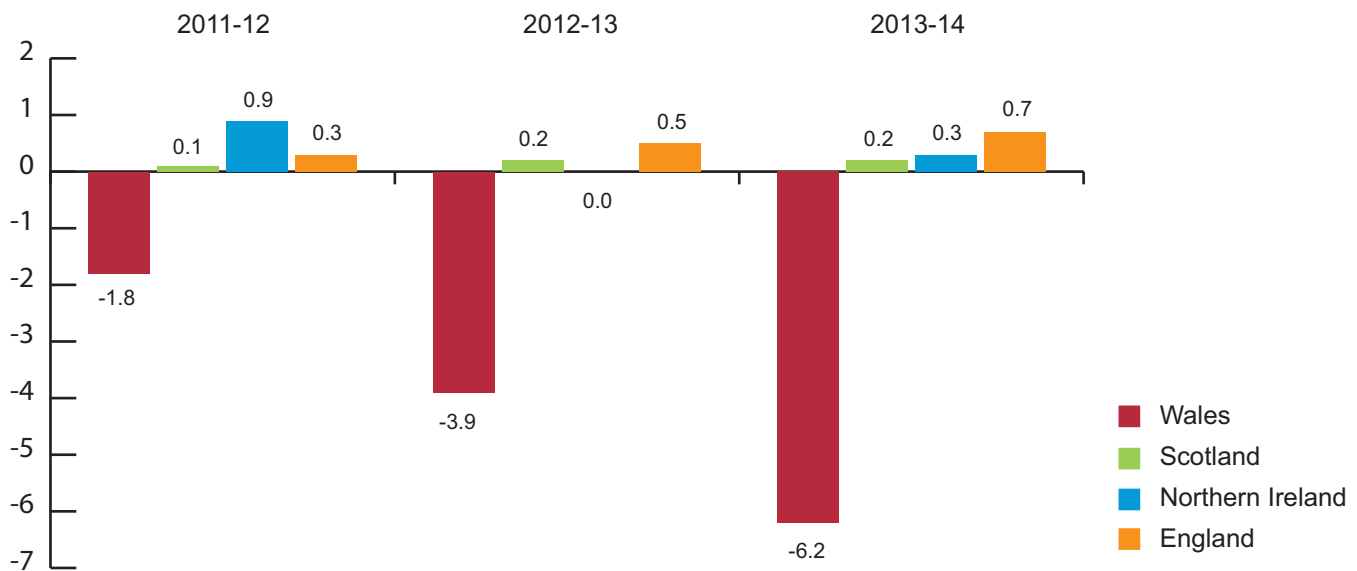
The NHS in Wales faces the toughest funding settlement in the UK, rising cost pressures and a significant funding gap for this financial year and beyond

Although the Welsh Government protected health spending in cash terms, the NHS in Wales faces a tougher funding settlement than the rest of the UK

1.7 The Welsh Government chose to protect health spending in cash terms. However Figure 4 shows that revenue spending on health and social services will be reduced in

real terms. The indicative NHS Delivery revenue budget (the funding provided for delivering NHS services) will reduce slightly less sharply than the overall budget for the Department. The NHS in Wales now faces greater financial pressures than other parts of the UK (Figure 5). In England, the UK Government intends to provide real-terms increases to the NHS revenue budget each year to 2014-15. The Scottish Government's revenue budget shows a real-terms increase in spending on NHS bodies in Scotland. The Northern Ireland Executive plans a real terms increase for 2011-12, and in the following years funding will stay around or above 2010-11 levels in real terms.

Figure 5 – Indicative real-terms changes in NHS revenue budgets from 2010-11 baseline (%)



Source: Wales Audit Office's analysis of budgets.

Note: As there are some differences in the budgets for each department, the comparison is indicative. The figures for Wales are based on the revenue budget for NHS Delivery in the Final Budget for 2011-12. The figure for Scotland is based on its revenue Departmental Expenditure Limit for Health. The figure for Northern Ireland is based on the revenue budgets for Hospital and Community Health. The 2010-11 baseline for England is based on the Department of Health's revenue budget for that year, as set out in the spending review. In its March 2011 budget, the UK Government used a revised 2010-11 baseline based on estimated expenditure.

The Welsh Government's recent draft budget proposals show an improved financial position, although the NHS in Wales still faces real terms cut, compared to 2010-11, of around 1.7 per cent in 2012-13 and 4 per cent in 2013-14 if those proposals are approved.

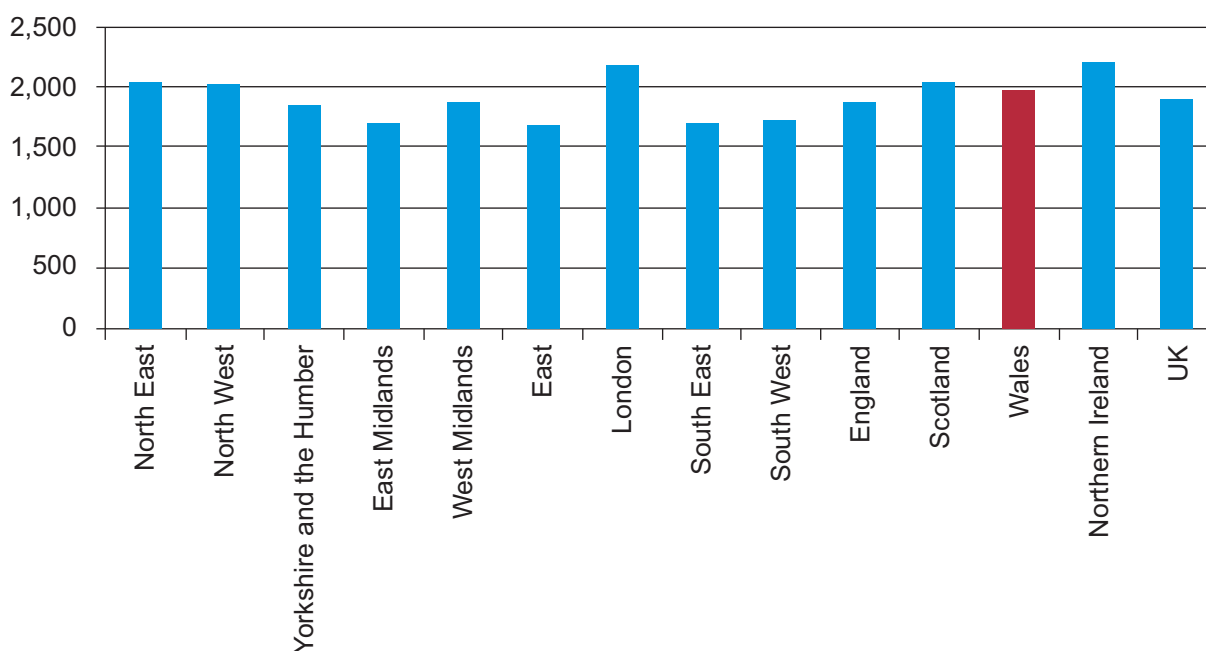


1.8 Figure 6 shows that spending on health per head of population in Wales (£1,975) was higher in 2009-10 than the UK average (£1,903).⁶ However, spending was slightly lower than other areas with broadly similar health and socio-economic characteristics, including Scotland (£2,044), Northern Ireland (£2,213) and the North East of England (£2,052). Although it is hard to be certain, the budget plans suggest that spending on health per head of population in Wales is likely to be the lowest of any of the countries in the UK by 2014-15.

A combination of real-terms budget reductions and projected cost and demand pressures means the NHS faces a growing funding gap

1.9 Public services across the developed world face growing pressures because of demographic changes. Longer life expectancy means that a growing proportion of the population are over 65. Clearly it is a good thing that people live longer. But there is a challenge to ensure that people stay healthy as well as living longer. With people living longer, but experiencing more health-related problems as they grow older, there continues to be an increase in demand for health and

Figure 6 – Spending on health per head of population 2009-10



Source: HM Treasury PESA 2011.

⁶ HM Treasury: *Public Expenditure Statistical Analyses (PESA) 2011*.

social care services, and an increased cost. The costs to the NHS in Wales of providing continuous care have increased by an average of 27 per cent a year between 2003-04 and 2009-10. The number of emergency patients admitted who are aged over 85 has increased by 22 per cent⁷. The Office of Budget Responsibility forecasts that across the UK, age-related spending will increase significantly as a proportion of Gross Domestic Product (GDP). **Figure 7** shows that health spending makes up the largest single element of age-related expenditure.

1.10 The NHS also faces rising demand and costs because of lifestyle factors. Recent research for the Welsh Government⁸ estimated the cost of obesity and alcohol to the NHS in Wales at £140 million in 2008-09. The study noted that across the UK the cost of obesity-related healthcare is likely to rise substantially in the future. It also noted that across the UK, the cost of alcohol-related conditions had more than doubled between 2001 and 2006-07.

Figure 7 – Office for Budget Responsibility projections for age-related public expenditure (percentage of GDP)

Description	2009-10	2019-20	2029-30	2039-40
Health	8.0	8.5	9.4	10.2
Long Term Care	1.2	1.4	1.7	2.0
Education	6.0	5.9	5.9	5.8
Pensions	5.5	5.3	6.1	6.8
Public Service Pensions	1.8	1.9	2.0	1.9
Total	22.5	23.1	25.1	26.6

Note: Figures are for the UK. Long-term care covers social-care expenditure on working-age and older people and excludes long-term care provided within the NHS which is included under health.

Source: Office for Budget Responsibility.

⁷ *Delivering a Five-Year Service, Workforce and Financial Strategic Framework for NHS Wales*, Welsh Government.

⁸ Phillips, Harper, Rance and Farr (2011) *Assessing the cost to the NHS associated with alcohol and obesity in Wales*, Welsh Government.



1.11 In addition to demographic and lifestyle factors, rising costs in areas like pay, new medicines as well as new surgical advances mean inflation in the NHS has historically run higher than inflation in the rest of the economy. In its Five Year Framework for the NHS, the Welsh Government sets out the estimated cost pressures on the NHS each year from 2010-11 to 2014-15 (Figure 8). These figures are based on a mixture of forecast demand growth and unit cost growth including inflation and rising costs of medicines. The five-year framework includes two scenarios, low growth in costs and high growth in costs, and reports that these forecasts have been tested extensively.

1.12 The NHS produced its five-year framework before the UK Spending Review and the subsequent Welsh Government budget.

It assumed annual cash-terms reductions in revenue of between three and four per cent. In fact, the Welsh Government was able to protect health spending in cash terms.

Figure 9 updates the Welsh Government cost-growth estimates in light of the Final Budget. It suggests a gap in the order of £570 million in 2013-14; much lower than the initial forecasts. Some of the variables in the calculation, notably non-pay inflation, are higher than they were when the Welsh Government produced the estimates. Also, they do not take account of potential demand as a result of the economic circumstances. Therefore, even the 'high-cost' scenario might understate the scale of the funding gap. However, the Welsh Government's 2012-13 draft budget proposals would reduce the funding gap for 2012-13 and 2013-14 (see note to Figure 9), if approved.

Figure 8 – NHS cost and activity growth assumptions

	Scenario 1 - High Cost Growth					Scenario 2 - Low Cost Growth				
	10/11	11/12	12/13	13/14	14/15	10/11	11/12	12/13	13/14	14/15
Activity growth¹	————— 2.9% p.a. —————>					————— 2.8% p.a. —————>				
-Demographic	————— 0.8% p.a. —————>					————— 0.8% p.a. —————>				
-Demand growth	————— 2.2% p.a. —————>					————— 2.1% p.a. —————>				
Unit cost growth	2.7	1.3	2.0	2.4	2.7	2.4	1.0	1.0	1.0	1.0
-Pay (70%)	3.0	1.0	2.0	2.5	3.0	3.0	1.0	1.0	1.0	1.0
-Non-pay (30%)	2.0	2.0	2.0	2.0	2.0	1.0	1.0	1.0	1.0	1.0
Total cost growth	4.4	3.3	3.8	4.1	4.4	3.7	2.6	2.6	2.6	2.6

1 Overall activity numbers are based on growth of individual service lines that are based on historical rates. Healthcare for London forecasts (informed by extensive clinical consultation) and local planning expertise. While overall growth seems similar in both cases, some service lines e.g. surgery are expensive and a small change in the activity can impact costs.

Source: Welsh Government.

1.13 The short-term funding gap in 2011-12 is likely to be higher than the **Figure 9** estimates suggest due to an underlying deficit the previous year. The NHS in Wales does not have a good track record of managing within the constraints of the budget set at the start of the year, despite the fact that it has enjoyed increased funding over the past 10 years. In 2010-11 that trend continues. The Department for Health and Social Services budget increased from £5.62 billion in 2009-10 to £5.87 billion in 2010-11 (although part of

the budget increase reflected technical accounting changes⁹). Despite the increase and reporting savings of around £300 million, the NHS needed an additional £110 million from Welsh Government reserves in 2010-11.¹⁰ As a result, in 2011-12, the NHS will need to manage the existing £110 million cost pressures that led to a requirement for extra funding in 2010-11 on top of the £140 million of new cost pressures estimated in **Figure 9**.

Figure 9 – Wales Audit Office’s analysis of the NHS funding gap

Revenue (£000s)	2010-11	2011-12	2012-13	2013-14
NHS Delivery (Wales) budget (cash terms)	5,332,150	5,368,048	5,368,049	5,381,817
% annual increase set out in the five-year framework				
Low cost	3.7	2.6	2.6	2.6
High cost	4.4	3.3	3.8	4.1
£ budget if it rose to meet forecast pressures				
Low cost		5,470,786	5,613,026	5,758,965
High cost		5,508,111	5,717,419	5,951,833
Funding gap				
Low cost		-102,738	-244,977	-377,148
High cost		-140,063	-349,370	-570,016

Source: Wales Audit Office analysis

Note: The figures are based on the Final Budget for 2011-12. If the Welsh Government’s draft budget proposals for 2012-13 are approved, the gap would be as shown below.

Funding Gap	2012-13	2013-14
Low cost	-121,064	-251,935
High cost	-225,457	-444,803

⁹ Such accounting issues include money transferred into the health budget from other departments to reflect changes in Ministerial portfolios and the UK-wide Clear Line of Sight programme to improve the transparency of government spending plans.

¹⁰ We intend to explore the funding gap, savings and additional funding in 2010-11 in more detail in a forthcoming Wales Audit Office report on NHS Finances.



Cuts in funding to Welsh councils are lower than elsewhere in the UK but some council services face significant budget reductions in the short term

Councils face significant cuts in their funding from central government, but fare better than the rest of the UK

1.14 Following the Final Budget, the Welsh Government announced its final revenue settlement for local councils in Wales. Overall, councils in Wales face a £155 million (3.8 per cent) real-terms reduction in their revenue funding from the Welsh Government in 2011-12 (Figure 10). The indicative figures show that, in real terms, the revenue funding from the Welsh Government will be around £283 million (seven per cent) lower in

2013-14 than 2010-11. The financial impact of the cuts in central government funding will vary between councils. Because local government funding is calculated using socio-economic factors, more affluent areas take a lower proportion of their income from the Welsh Government.

1.15 Councils in Wales face less severe cuts than councils in other parts of the UK (Figure 11). Direct comparison is difficult, because local government is funded in slightly different ways, and has slightly different responsibilities in each country. Nonetheless, we are confident that the figures underpinning Figure 11 are sufficiently similar to provide an indicative comparison. Figures for England show that such funding will be 7.5 per cent lower in 2011-12 than 2010-11, in real terms. In Scotland, local government faces a 4.9 per cent real-terms cut in central government revenue in 2011-12. Differences in the way the budgets are presented meant we could not make a comparison with Northern Ireland.

Figure 10 – Real-terms reduction in central government funding for councils

Unitary authority	2011-12	2012-13 (indicative)	2013-14 (indicative)
Isle of Anglesey	-4.10% -£3.9 million	-6.55% -£6.2 million	-7.97% -£7.6 million
Gwynedd	-4.10% -£7 million	-6.17% -£10.5 million	-7.70% -£13.2 million
Conwy	-4.10% -£6.0 million	-6.33% -£9.3 million	-7.86% -£11.6 million
Flintshire	-4.10% -£7.7 million	-6.54% -£12.3 million	-7.98% -£15.0 million
Pembrokeshire	-4.10% -£6.7 million	-6.10% -£9.9 million	-7.50% -£13.0 million
Neath Port Talbot	-4.10% -£8.2 million	-5.82% -£11.6 million	-7.05% -£14.1 million
The Vale Of Glamorgan	-4.10% -£6.3 million	-6.25% -£9.6 million	-7.53% -£11.5 million

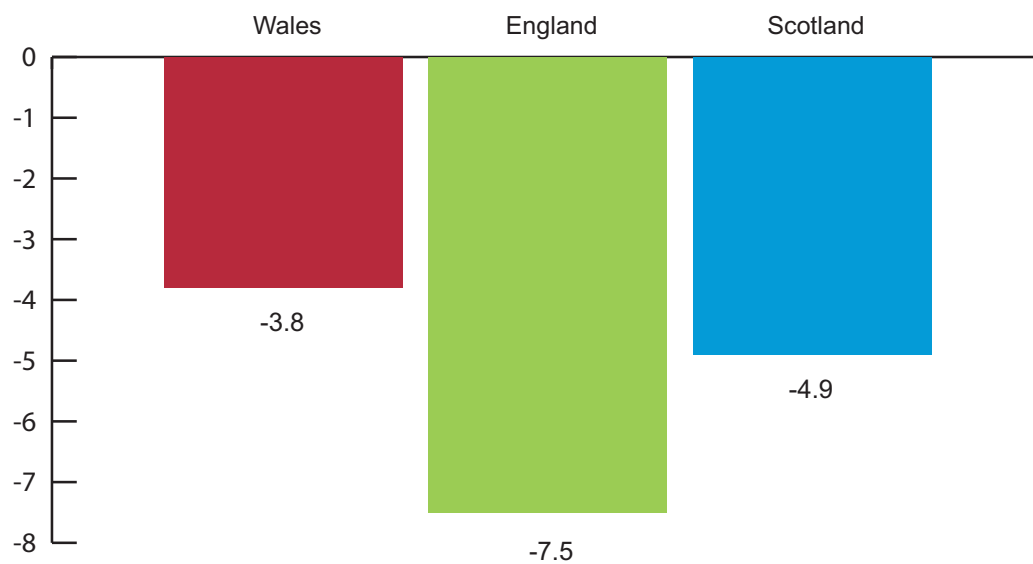
Figure 10 – Real-terms reduction in central government funding for councils (continued)

Unitary authority	2011-12	2012-13 (indicative)	2013-14 (indicative)
Rhondda Cynon Taf	-4.10% -£14.3 million	-5.97% -£20.1 million	-7.23% -£25.3 million
Merthyr Tydfil	-4.10% -£3.6 million	-6.22% -£5.5 million	-7.42% -£6.5 million
Caerphilly	-4.10% -£10.5 million	-5.78% -£14.8 million	-7.01% -£17.9 million
Blaenau Gwent	-4.10% -£4.5 million	-6.56% -£7.2 million	-7.86% -£8.7 million
Torfaen	-4.10% -£5.4 million	-6.54% -£8.6 million	-7.86% -£10.4 million
Monmouthshire	-4.10% -£4.0 million	-7.59% -£7.4 million	-9.16% -£9.0 million
Newport	-4.10% -£8.1 million	-6.14% -£12.2 million	-7.35% -£14.5 million
Denbighshire	-4.02% -£5.6 million	-5.61% -£7.8 million	-6.95% -£9.6 million
Swansea	-3.86% -£11.7 million	-5.37% -£16.3 million	-6.56% -£19.9 million
Bridgend	-3.84% -£7.0 million	-5.33% -£9.7 million	-6.56% -£11.9 million
Carmarthenshire	-3.66% -£9.2 million	-5.20% -£13.1 million	-6.46% -£16.3 million
Powys	-3.65% -£6.6 million	-5.61% -£10.2 million	-7.15% -£13.0 million
Wrexham	-3.63% -£5.9 million	-5.25% -£8.6 million	-6.49% -£10.6 million
Ceredigion	-3.13% -£3.2 million	-5.04% -£5.1 million	-6.54% -£6.7 million
Cardiff	-2.39% -£9.4 million	-3.69% -£14.6 million	-4.56% -£18.0 million
Total Unitary Authorities	-3.81% -£154.9 million	-5.69% -£231.4 million	-6.97% -£283.4 million

Source: Wales Audit Office's analysis of Welsh Government data.



Figure 11 – Real-terms reduction in revenue funding from central government in 2011-12 (per cent)



Note: Figures for Wales are based on Welsh Government data on Aggregate External Finance. Figures for England combine the Revenue Support Grant Settlement and the Direct Schools Grant. The figure for Scotland covers the Direct Resource Grant as set out in the Scottish Government's budget.

Source: Wales Audit Office analysis of budgets.

All but one Welsh council has increased council tax, whereas England and Scotland have had a council tax freeze

1.16 Councils in Wales also have more scope to increase council tax income than in some other parts of the UK. The Welsh Government has provided councils with £32 million in 2011-12, which they have the option of using to support a council tax freeze, or spend on other services. In England and Scotland, there has been a freeze on council tax. In England, councils received an extra £650 million in total as an incentive to freeze council tax. In Scotland, councils had a choice of signing up to a council tax freeze alongside

other policy priorities. Any council not signing up faced a significant funding cut. In the event all Scottish councils signed up.

1.17 Welsh councils set their budgets in February and March 2011 and almost all took the option of increasing council tax levels. **Figure 12** shows the levels of increase for an average Band D household in each council. Caerphilly County Borough Council was the only council to freeze council tax levels. Nevertheless, in 2011-12 the average band D council tax in Wales (£1,162) remains lower than in England (£1,439) although the recent increase means it is now slightly higher than Scotland (£1,149).

Figure 12 – Increase in average band D council tax (percentage increase in cash terms)

Year	2011-12			
Description	County council council tax (excluding community councils)	Community council council tax	Police council tax within county area	Total council tax for billing authority area
Authority				
Gwynedd	3.90	2.84	3.98	3.89
Newport	3.90	8.62	3.70	3.88
Bridgend	3.77	-0.28	5.00	3.83
Isle of Anglesey	3.71	3.12	3.98	3.74
Carmarthenshire	3.74	2.43	4.22	3.74
Conwy	3.71	1.95	3.98	3.71
Swansea	3.40	1.44	5.00	3.60
Vale of Glamorgan	3.30	1.30	5.00	3.47
Merthyr Tydfil	3.20	2.02	5.00	3.41



Figure 12 – Increase in average band D council tax (% increase in cash terms) (continued)

Year	2011-12			
Description	County council council tax (excluding community councils)	Community council council tax	Police council tax within county area	Total council tax for billing authority area
Authority				
Blaenau Gwent	3.20	0.17	3.70	3.23
Ceredigion	3.00	3.67	4.22	3.22
Rhondda Cynon Taf	2.95	1.90	5.00	3.19
Flintshire	3.00	3.13	3.98	3.18
Wrexham	3.00	2.65	3.98	3.17
Powys	2.99	2.03	4.22	3.16
Denbighshire	2.90	2.38	3.98	3.06
Pembrokeshire	2.90	-0.85	4.22	3.06
Neath Port Talbot	2.90	-1.14	5.00	3.03
Torfaen	2.99	0.74	3.70	3.03
Monmouthshire	2.90	2.55	3.70	3.01
Cardiff	1.94	5.23	5.00	2.39
Caerphilly	0.00	1.62	3.70	0.63

Source: Local Government Finance Statistics, Welsh Government.

Overall, councils plan real-terms cuts across all major service areas, but some service areas face substantial cuts in 2011-12 and there is significant variation between councils

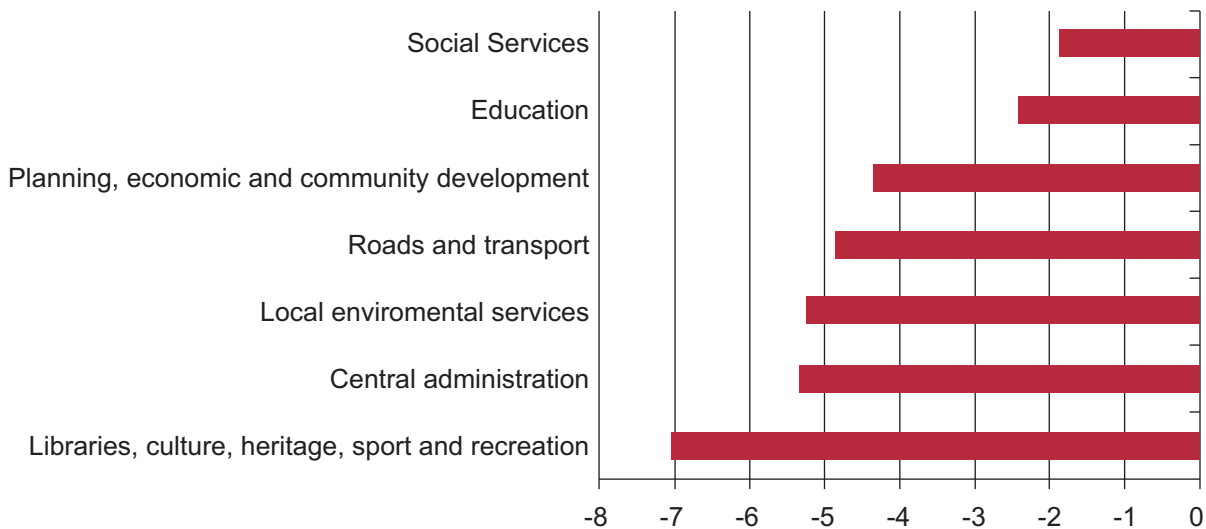
1.18 Figure 13 provides an indication of the cuts to council services' budgets. It shows that while, overall, councils plan to make real-terms cuts across all of the main service areas in 2011-12, some services face a substantially more challenging time. Councils have afforded the greatest protection to spending on social services and education. The greatest cuts fall on libraries, culture, heritage, sport and recreation services. Within the overall figures, there is some significant variation between councils. Just one council's plans show an increase in education spending in real terms. And six of the twenty-two plan real-terms increases on social-care spending.

Councils have the option of drawing on reserves although this is not a sustainable long-term solution

1.19 The Local Government Finance Act 1992 requires local authorities to have regard to the level of reserves needed for meeting estimated future expenditure needs. In March 2011¹¹ Welsh councils held reserves totalling around £1.3 billion, of which:

- a** £252 million is restricted for use on capital expenditure;
- b** £74 million is held by schools and is not available for use by the council more generally; and
- c** £96 million is ring-fenced for use for housing purposes.

Figure 13 – Indicative real-terms budget cuts to key council services between 2010-11 and 2011-12 (%)



Note: Because councils reported their budgets for 2010-11 differently from 2011-12, these figures should be treated as illustrative of the level of cuts.

Source: Wales Audit Office analysis of StatsWales data.

¹¹ The figures are based on a Wales Audit Office analysis of the draft 2010-11 accounting statements of the 22 Welsh councils and may change when the accounts are finalised.



1.20 £764 million of the remaining £919 million revenue reserves are earmarked for specific purposes. These earmarked reserves are set aside by councils as part of their financial planning, to meet predicted future requirements. Councils also set aside what they consider to be prudent unallocated general reserves based on an assessment of their internal and external strategic, operational and financial risks. In March 2011, councils held £155 million in general reserves (approximately 1.6 per cent of councils' annual gross revenue expenditure). If deemed prudent, councils can decide to use part of their reserves to help manage short term pressures and/or, as some councils are already doing, to invest in new ways of working that could ultimately reduce the costs of service delivery. However, using reserves to meet recurrent revenue funding shortfalls is not a sustainable solution and councils must have due regard to maintaining prudent level of reserves to manage future risks and requirements.

Councils have compensated for large cuts in capital funding from central government in the short term but the approach, particularly additional borrowing, is not sustainable in the medium to long term

1.21 Capital funding to councils from the Welsh Government and other UK Government Departments falls by around 30 per cent, in real terms, in 2011-12. Also, there has been a 20 per cent reduction in central government supported borrowing. Councils have managed to make up much of the shortfall, through a major increase in European Union structural funding, by transferring some capital expenditure to revenue accounts and also through borrowing. With revenue budgets

under increasing pressure, there is limited scope for councils to continue to fund capital programmes from their revenue. Councils are forecasting a 28 per cent cash reduction in spending on capital programmes in 2012-13 and there is considerable uncertainty about how capital programmes will be funded in the medium to long term. Councils are particularly concerned that using revenue to support mainstream capital programmes reduces their ability to invest in supporting innovative and more efficient ways of working.

Fire and rescue authorities are funded through contributions from councils and face varying levels of budget cuts

1.22 The three Fire and Rescue Authorities (FRAs) in Wales are primarily funded by contributions from the councils in the area that they cover. Each FRA sets its own budget, in discussion with the constituent councils. They face real-terms cuts of between 2.4 and 4 per cent. In total, the FRAs face a real terms cut of 3.7 per cent (£5.6 million) in 2011-12.

Councils face known cost pressures as a result of rising demand, particularly in social services

1.23 The same demographic factors described above in relation to health (paragraph 1.9 and Figure 7) also create increased demand and cost pressure for social services. Figure 7 shows that over the next 30 years, spending on social care will almost double as a proportion of UK GDP. Several recent reports note that the approach, found in Wales and other areas, of tightening eligibility criteria to restrict access to care services for those with low or moderate support requirements is unsustainable because it leaves people with unmet needs.¹²

¹² See the Report of the Independent Commission for Social Care in Wales, *Sustainable Social Services: A Framework for Action*, Commission on Funding of Care and Support: call for evidence.

1.24 Social services also face growing demand for services for children. Over the past decade there has been a 44 per cent increase in the number of children being taken into care in Wales. This includes an increase of 10 per cent between 2008-09 and 2009-10. The reasons behind the increase are complex. In part it could be a real increase in mistreatment and abuse of children. In part, it could be because social services are intervening more appropriately to protect children from harm.

The economic climate may result in an increase in demand from vulnerable groups at a time when resources are declining

Public spending in non-devolved areas, such as social security and policing, is set to fall, with a potential impact on devolved services

1.25 Almost half of public spending in Wales is not actually devolved to the Welsh Government. The bulk of this non-devolved spending is social security payments. The UK Government plans to make significant changes to the social security system, which will impact on people in Wales. The Spending Review set out the UK Government's intention to reduce the overall social security bill. A major plank of reform includes moving people from disability benefits to job-seekers benefits. It remains unclear what the implications will be for public services in Wales, but it is possible that some changes may create extra demand and cost pressures. There could be direct pressures on services like training and indirect pressure on voluntary sector advice and support services that are funded by the public sector. Also the impact is

unclear on council services, such as housing, where benefit eligibility and levels form part of the criteria for accessing services.

1.26 Police forces in Wales also face significant cuts, with potential implications for other public services they work with in Wales. They face a 20 per cent real-terms cut in central government funding between 2010-11 and 2014-15. Compared to 2010-11, real-terms central government funding will be 6.1 per cent lower in 2011-12 and 13.2 per cent lower in 2012-13. As **Figure 12** shows, police authorities in Wales have sought to bridge some of the gap through increasing the police precept in the Council Tax, with rises of between 3.7 and 5 per cent. However, the precept makes up just a quarter of the total police budget, so the rise in the precept will only make up a small part of the cut. Up to 80 per cent of police spending is accounted for by staff costs and Welsh police forces expect a reduction in the number of staff they employ, with some expecting reductions in officer numbers (see **Part 2**). Any consequential impacts for other public services working alongside the police to support community safety are as yet unclear.

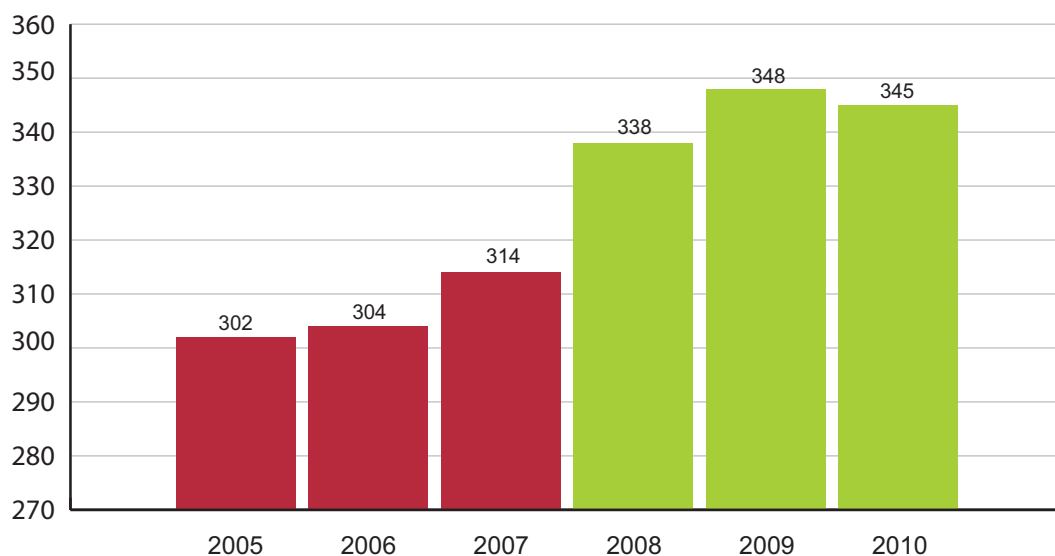
Public-sector and related employment in Wales is likely to fall, after a period of sustained growth which may result in additional demand for some services

1.27 Public-sector employment has risen between 2005 and 2010 (**Figure 14**). Some¹³ of the increase is accounted for by the fact that some banks were brought into public ownership during 2007 and 2008 and their employees became classified as public-sector workers. There was a decrease in the number of public-sector workers between 2009 and 2010.

¹³ We estimate this to be around 7,000 people in Wales.



Figure 14 – Public-sector employment in Wales (thousands)



Source: Stats Wales/Office of National Statistics

Note: These figures are illustrative. Figures for 2005 to 2007 are not directly comparable to those for 2008 onwards due to a change in the methodology for producing the statistics.

1.28 The Office for Budget Responsibility (the OBR) predicts that across the UK, there will be 320,000 fewer jobs in the public-sector workforce. We have applied the OBR's method for calculating this figure for Wales, to estimate a total of 21,000 public-sector job cuts (Figure 15). This is an estimate, and actions of public services to minimise job losses could have the potential to reduce this number. In addition to the potential direct job losses, there is a further multiplier effect on the wider jobs market as a result of falling levels of procurement and spending in the private sector. Pricewaterhousecoopers estimate that in Wales, there will be a total of 50,000 job losses in the private and public sector, as a result of the spending cuts.¹⁴

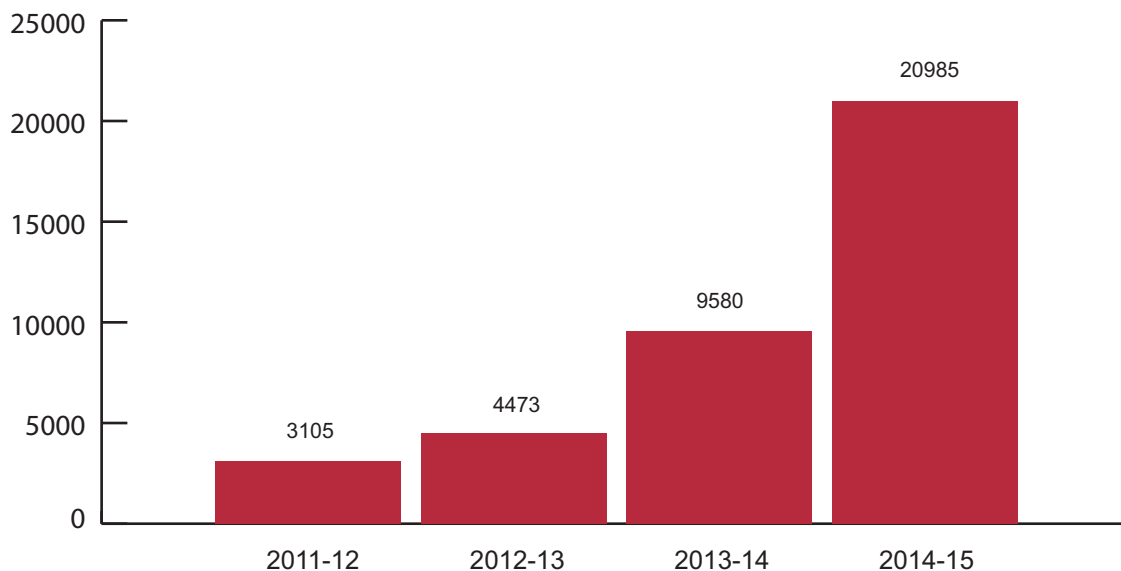
1.29 There will be a challenge to replace the lost jobs in the public sector through new private-sector jobs. The private sector in Wales was particularly hard hit during the recession. Between early 2009 and early 2010, private sector employment in Wales fell by 5.4 per cent (52,000 jobs)¹⁵. This compares to a 1.1 per cent fall across the UK as a whole over that period. Since then, employment levels in Wales have increased ahead of the rest of the UK. The number of people in employment in Wales increased by 1.8 per cent (an extra 24,000 people) between the three months to June 2010 and the three months to June 2011, compared to a 1.1 per cent increase across the UK.¹⁶ Recruitment freezes in the public sector over 2010-11 mean that a significant proportion of the increase is likely to be due to an increase in private employment.

¹⁴ Pricewaterhousecoopers (2010) *Sectoral and regional impact of the fiscal squeeze* by John Hawksworth and Nick Jones, PwC Public Sector Research Centre, published on 13 October 2010 and available to download from: www.psrc-pwc.com

¹⁵ Source: ONS, *Regional Analysis of Public Sector Employment*, September 2010.

¹⁶ Source: ONS, *Labour Force Survey data*, July 2011.

Figure 15 – Cumulative public-sector job losses in Wales using the OBR formula



Source: Wales Audit Office analysis using the OBR formula and ONS data

Efficiency savings alone are unlikely to bridge the gap and public services will need good governance, bold leadership and public engagement to deliver real cost reductions and priority-based cuts

1.30 The funding position for many public services is better than anticipated. The Welsh Government had prudently planned for a worst-case scenario, based on a three per cent cash-terms cut in revenue every year, and a 10 per cent year-on-year cut in capital funding. Other public services including some councils and NHS bodies had also used these planning assumptions. In fact, the revenue position is considerably more positive for

public services in Wales, although the capital situation is broadly as predicted in the worst-case scenario.

1.31 While planning for the worst-case scenario was prudent, there is a danger that public services may now breathe a sigh of relief, knowing that things are not as bad as they could have been. In fact, the funding position is in line with our estimate last year. At that time, we were clear that budget cuts at the level now expected would require public services to make significant changes and tough choices in order to reduce their costs. Our assessment has not changed.

1.32 The ideal scenario is for public services to bridge the funding gap through reforming services to deliver efficiency savings. Such an approach would mean reducing costs sufficiently to bridge the funding gaps while



delivering the same or better quality and level of service. There are opportunities for public services to improve efficiency in a range of areas, many of which are set out in part two, and regardless of the financial climate, all public services should be continuously seeking ways to improve. Transformational change – developing more cost effective business processes and service models – is essential if public services are to deliver improved outcomes for people in the future. All public services will need to fundamentally review the way that they work, focusing in particular on identifying and designing out activity that does not contribute real value: providing the high-quality services that people want and need and improving outcomes for the wider population. Transformation is not just about radically changing services: it is also about enabling a culture of continuous improvement on a day-to-day level. Transactional savings, through better procurement and from better management of assets, are also important ways of reducing or avoiding costs without reducing service quality or harming outcomes.

1.33 However, it is important to balance ambition and realism. In practice it is unlikely that public services will be able to entirely bridge the financial gap they face in the next few years through efficiency savings alone. While large efficiency savings may, in theory, be possible across public services, actually delivering them is often difficult. There is an extensive body of evidence showing that change projects and programmes in the private sector and public sector alike suffer from 'optimism bias'; those involved expect them to deliver much more than they do in a much shorter timeframe. Treasury guidance explicitly warns public services to adjust for such optimism in their calculations.

1.34 The experience of efficiency programmes in Wales and elsewhere in the UK suggests that public services struggle to deliver the cashable savings they expected. Often, that is because delivering real efficiency savings requires changes in the way organisations work together and the way their leaders, managers and frontline staff think and behave. Also, it may involve changes in the ways that service users can access services. In some cases, staff, service users and other stakeholders may actively resist and hamper change, especially if they have not been engaged in designing new ways of working. It can take time to secure the necessary buy-in and support.

1.35 In addition, it can be difficult to translate service changes into hard cash savings. Often any capacity freed up ends up being used to provide a service to more people or improve the service, rather than actually releasing cash. The bulk of the costs of delivering a service are usually tied up in staff costs. Unless the change leads to overall reductions in staff cost, the savings do not get realised. Of course, it can be easier to secure cost savings through areas like procurement, where costs are bound up in products rather than people. But even then some change is required to get staff within an organisation familiar with and fully using the procedures. Such behavioural change takes time and effort to deliver.

1.36 With efficiency savings unlikely to bridge the full gap in the short term, it is likely that public services will need to make some form of cuts. These tough choices could involve ending particular projects or programmes, reducing the level of some services or reducing or restricting access to some services. Such choices are not easy. Public services will need to base decisions on clear priorities and

robust analysis of potential impacts on service users and wider outcomes. Not only is assessing the impact intrinsically important, but following recent legal developments¹⁷, making cuts without fully assessing the potential impacts leaves public services open to legal challenge. They will also need to take account of impacts on other services; there is little benefit in one part of the public sector making savings by re-directing demand and cost to another part of the public sector.

1.37 Delivery of the changes and tough decisions that public services must make will require careful and bold leadership. Leadership is not restricted to a small number of senior politicians and managers. Leaders include back-bench and opposition politicians who have an important community leadership role, as well as managers who are responsible for leading teams of staff at the front-line. There is no one-size-fits-all model of leadership and public service leaders use a variety of approaches. Nonetheless, there are some common challenges that all leaders will need to face up to in the coming years:

- a** setting the tone, communicating the need for change in general, and the rationale for specific planned changes;
- b** encouraging managed risk taking, tapping in to the knowledge and creativity of staff by encouraging them to innovate and learn from practice elsewhere to find new ways of working that can save money;
- c** engaging the public, as a minimum to explain why decisions have been taken and changes implemented, and ideally to involve the public in shaping those decisions and changes;
- d** thinking and acting on their feet: identifying and overcoming the many barriers to

change that exist and knowing when to adapt and when to stand firm in the face of opposition;

- e** sustaining a relentless focus on realising the benefits of change programmes, challenging themselves and others to ensure that they actually deliver the planned cost reductions while minimising the impact on service users; and
- f** keeping track of the consequences of their decisions, especially on the most vulnerable, and being prepared to change where necessary if their decisions are having negative or unintended consequences.

1.38 With change and tough choices the order of the day, effective governance will be even more critical across public services. If the public is to have confidence in the changes, public services will need to demonstrate that their plans have been subject to proper scrutiny and challenge by management alongside well-informed, active, and engaged politicians. To support good governance, managers and staff will need to provide high quality business cases, with robust financial appraisals and evidence to support change. All of those involved in governance, including elected politicians and non-executive members of boards and committees, have a responsibility to challenge and test those business cases robustly, taking into account the impacts and benefits for the wider public service as well as for their local area. There must also be scrutiny of delivery. The public needs to have confidence that public services are being challenged on the pace of delivery, the extent to which they are delivering real cash savings and the extent to which they can adapt to any unforeseen issues, including changing their plans where

¹⁷ The case of R (W) v Birmingham City Council (2011)
<http://www.judiciary.gov.uk/NR/rdonlyres/7852C851-129F-4DFB-89C1-C495BD08DCBC/0/birminghamcitycouncil19052011.pdf>



there are negative and unforeseen consequences for service users and citizens. As we said in our previous report, public services need to publish more information about how well they are performing, so that citizens can themselves understand and challenge performance.

Public-sector wage and recruitment freezes and voluntary redundancy schemes will help bridge the gap, but effective workforce planning and communication are required to manage significant risks

1.39 For most public services, their main controllable cost is their wage bill. As a result, if they are to cut costs it is inevitable that public services will need to look at cutting staff costs. The two main mechanisms for reducing staff costs are to reduce pay and reduce the number of employees (or reduce their hours). Both options are being used across public services in Wales, and have potential benefits in terms of bridging the funding gap, but also have limitations and carry risks.

While wage freezes will save some money, it may not be as much as some expect, and public-service leaders will need to carefully manage the impact on staff morale and industrial relations

1.40 It may seem that a two-year wage freeze, as the Chancellor of the Exchequer announced, would insulate the public sector from wage inflation. However, not all of those working in public services will actually have their pay literally frozen. For example, many public-

sector workers earning less than £21,000 will receive a £250 increase. Also, many public-sector employees' terms and conditions include annual pay increases, for example on the basis of good performance, or moving within a pay band. These increases happen anyway, regardless of the pay freeze. The OBR calculates that, despite the announced pay freeze, the average cost per public-sector worker across the UK will increase by 1.8 per cent in 2011-12, 0.8 per cent in 2012-13 and by 3.7 per cent in 2013-14 and 2014-15. So while a wage freeze may slow down the rate of wage inflation, it will not do away with it all together.

1.41 There are risks associated with a sustained public-sector pay freeze. A pay freeze is equivalent to a drop in living standards. With consumer price inflation at relatively high levels, the extent of the decline in living standards is likely to be noticeable. There is a real possibility that cuts in living standards could negatively impact on staff morale. This creates two key risks. The first is that industrial relations will deteriorate without effective management and communication, disrupting the delivery of public services. The second risk is that poor morale discourages the staff engagement and support that is critical to the success of many of the kinds of change initiatives that public services will need to go through in the next few years. The Welsh Government told us that it expects its social partnership approach to working with trade unions to help in managing the difficult industrial relations environment.

1.42 There is a small risk that wage freezes may inhibit the public sector's ability to compete with the private sector to recruit essential staff. The Institute for Fiscal Studies (IFS)¹⁸ reports that in Wales, those in the public

¹⁸ Institute for Fiscal Studies (2010), *The IFS Green Budget February 2011*, www.ifs.org.uk

sector are paid an hourly rate around 10 per cent more than those in the private sector for comparable work. In London and the south-east of England, there is virtually no pay differential according to the IFS. While a two-year pay freeze will reduce the pay differential in Wales, it will remain. The IFS analysis shows that if the pay freeze is extended for an additional two years, comparable wages would be higher in the private sector, and public services in Wales might then struggle to compete for the right staff. Despite the existence of the differential, there remains a risk that there may be some specific challenges in areas like ICT, where skills are highly in demand. There is some evidence from our local audit work that public services sometimes struggle to recruit and retain the highly skilled ICT staff they want and need.

Recruitment freezes and voluntary redundancies offer scope for savings but good workforce planning and management are required to avoid skills gaps impacting on the quality of services

1.43 As well as pay freezes, many public bodies are planning to manage down staff costs through not replacing staff who leave voluntarily or through retirement. This is likely to yield savings, but there are several reasons why this may not have as large an impact as hoped. Firstly, the abolition of the retirement age is likely to result in fewer people moving on at the traditional retirement age. Surveys by the Chartered Institute for Personnel and Development (CIPD)¹⁹ show that the proportion of the workforce moving on due to retirement has fallen significantly. Further, there is evidence that staff turnover is reducing as people look to consolidate their

employment position in times of uncertainty. The CIPD surveys show that turnover in the public sector fell from 13.5 per cent in 2008, to 8.5 per cent in 2011. Over the same period, there was a reduction in the rate of staff leaving voluntarily from 9.4 per cent to 3.4 per cent.

1.44 To encourage staff to move on, some organisations offer incentives through early retirement or voluntary severance schemes. However, there are significant up-front costs involved in such approaches. It can take time for the savings to outweigh the initial costs. Also, of course, organisations need to be able to afford the up-front payments in the first place.

1.45 The danger of managing down staff costs by letting staff go and not replacing them is that it can be quite random, with staff being lost on the basis of who wants to leave, rather than the business needs of the organisation. It is quite likely that those keen to leave might be people with highly prized and needed skills that would be welcomed in other parts of the economy. The net result is a serious risk that public services end up with skills gaps in some key delivery and leadership areas. There is no simple solution to the challenge of reducing staffing costs. Sound workforce planning will be required to make sure that services do not suffer as a result of skills gaps. That means organisations will need to:

- a** robustly identify the service demands they are likely to face;
- b** identify the resources needed to deliver priority outcomes;
- c** work out the skills and capacity they need to meet those demands and priorities;

¹⁹ Chartered Institute for Personnel and Development (2011), *Resourcing and Talent Planning*, www.cipd.co.uk



- d** have a clear system for re-skilling and redeploying people displaced as a result of service transformation; and
- e** take decisions on the basis of business needs as well as the need to reduce costs.

1.46 Public services will also need to explore options other than losing staff. For example, there may be scope to look at making savings through reform of terms and conditions, which vary across public services. There is also potential to make cost reductions through more flexible working, and encouraging staff to adopt shorter working weeks, subject to business needs. These kinds of approaches can help to reduce costs while reducing the number of job losses.

Part 2 – Public services are prepared for funding cuts, however, while all will be seriously tested as they move to actually delivering real cost reductions, some face greater difficulties

2.1 This part of the report looks at the preparations of the Welsh public service to face the forthcoming cuts. In particular it draws on our recent audit work to look at how they are planning to deal with the cuts and any lessons that could help them to improve their response. For most sectors it looks in particular at service transformation and financial and workforce planning as key processes through which services can identify how exactly they will reduce their costs while minimising the impact on service users and wider outcomes. In the section on central government, we consider the lessons and findings from our national value for money studies in the context of the challenges facing the Welsh Government and its sponsored bodies.

The Welsh Government has a programme for making internal savings but faces particular challenges in working with others to deliver its strategic goals cost effectively

The Welsh Government is reporting savings from its internal efficiency programme and plans to reduce staff and administrative costs

2.2 The Welsh Government has set up a programme for reducing its own running costs. It intends to reduce its own central services budget by £77 million in real terms by 2013-14.²⁰ It launched the 'Managing with

less' programme in February 2010, with the intention of engaging staff in identifying ways to reduce costs. The Welsh Government estimates that the programme has saved around £14 million as at the end of May 2010. We have not verified these reported savings.

2.3 In evidence to the Public Accounts Committee in July 2010, the Permanent Secretary reported that the Welsh Government intended to reduce staff costs, particularly through reducing the number of temporary and casual staff. Its budget shows staff costs falling from £214 million in 2011-12 to £193 million in 2013-14. Office of National Statistics figures show that the total number of staff employed in the Welsh Government fell from 6,020 in September 2009 to 5,560 in March 2011: a reduction of almost eight per cent. Over the same period, the number of casual and temporary staff fell from 310 to 170 people.

2.4 Many staff have left through the Welsh Government's early severance/voluntary retirement schemes. The Welsh Government reports that, in total, 637 people agreed to leave under these schemes during 2010-11. The total cost has been around £29.9 million. The Welsh Government calculates that the initial costs will be recouped in 14 months. After then it expects to save around £26 million a year off the pay-bill. The scheme continued into 2011-12 and nearly 300 more people will leave under early exit terms, at a cost of about £15 million and the Welsh Government expects recurring annual savings of about £13 million. The Permanent Secretary told the Finance Committee in July

²⁰ Source: Wales Audit Office analysis of Welsh Government budgets.



2010 that it is impossible to mitigate fully the risk of leaving departments with skills gaps when operating a voluntary scheme, but that decisions had been made in such a way as to minimise the impact on the business.

With an increased focus on delivery, the Welsh Government will need to strengthen and clarify relationships with those organisations, especially councils, that it relies on to deliver its strategic goals cost effectively

2.5 As well as pressure on its running costs, there is considerable pressure on the Welsh Government to get more value from the money that it passes on to other organisations. Since the May 2011 election, the First Minister has been clear that the Welsh Government intends to increase its focus on delivery. In large part, the Welsh Government relies on other organisations, for example, councils, health boards, sponsored bodies (like the Arts Council of Wales), as well as private companies and voluntary organisations, to actually deliver its policy and strategic priorities.

2.6 Several studies we have carried out recently have touched on the key issue of how the Welsh Government manages its relationships, particularly with local government, to deliver its objectives. Our work suggests that in several areas it has struggled to effectively strike a balance between prescription and local flexibility, leading to confusion for both the officials in central government and the organisations working on delivery. Several examples from recent reports illustrate this point in relation to local authorities (Figure 16) as well as many of our previous reports on topics such as *Communities First* and *Increasing Physical Activity*.

2.7 We also found evidence that the Welsh Government Sponsored Bodies (WGSBs) sometimes found the relationship with the Welsh Government difficult. As part of our financial audit work, we ran workshops with the Directors of Finance of WGSBs. These workshops suggested that the AGSBs viewed the stance taken towards them by the Welsh Government as both confused and overly prescriptive. They welcomed the Welsh Government's goal of allowing greater freedom and flexibility for WGSB. However, they reported that individual departments and divisions were continuing to issue detailed management instructions that contradicted the aspiration for greater freedom and flexibility. We have not verified the WGSBs' concerns, about mixed messages and inconsistencies in the ways that different parts of the Welsh Government related to the WGSBs.

2.8 The Welsh Government has taken, or is taking, steps to improve the situation in the examples identified here. But there is merit in seeking to apply the lessons learnt more widely to ensure that the Welsh Government takes a considered and explicit approach to managing the relationships involved in delivering each of its goals, strategies and programmes. In some cases, that may involve being directive and monitoring closely. Such an approach is appropriate for high risk areas in order to avoid, for example, the problems we found with the Communities First Scheme in Plas Madoc. In some cases an appropriate approach may involve providing support to develop capacity, as it has started to do with the locally managed transport projects it funds. In others it may mean being more hands off and adopting a flexible approach. The key factors are from the outset:

Figure 16 – Examples of the lack of clarity in relationships between the Welsh Government and councils

We found in our work on housing for adults with mental health needs, the Welsh Government decided to adopt a 'light touch' performance management and governance regime. In practice, we found that the Welsh Government had put in place some of the mechanisms associated with a more prescriptive approach: a targets and monitoring regime. However, few councils submitted the required information. Where they did, the information was not comprehensive and did not relate directly to the targets. The Assembly Government did not scrutinise or challenge these reports, nor did it engage effectively in other actions to assess progress in delivering targets.

Our work on Major Transport Projects found that the Welsh Government had not set out clearly enough the basis of its involvement in projects funded through its Transport Grant mechanism but delivered by local government. Engagement by Welsh Government officials in these projects was, as a result, inconsistent. The Welsh Government had also not made clear its expectations in terms of local project management arrangements for those schemes funded by the Transport Grant. This was due, in part, to a previously established but since challenged view that it was not the Welsh Government's place to exercise close control over local authorities' delivery of these projects. In written evidence to the Public Accounts Committee, the Welsh Government acknowledged that the more limited top-down control exercised in the past had contributed to the increasing costs of the Transport Grant funded major projects featured in our report when compared with early estimates. However, our report and the Welsh Government's evidence to the Public Accounts Committee pointed to the action that had been taken over the previous two years to exercise greater control over the Transport Grant programme and the future delivery of the new Regional Transport Plans.

We found the Welsh Government had not set a clear direction in relation to school building improvement. The Welsh Government provided councils with investment of £560 million to support both refurbishing schools and building new facilities, to ensure that schools were 'fit for purpose'. Because the Welsh Government did not specify what 'fit for purpose' meant, local authorities were uncertain about the quality of school buildings that they should aim to achieve and consequently were uncertain about how much they needed to spend. We also found that despite requiring all councils to produce education asset management plans by 2003, in 2010 many councils had no such plans and the Welsh Government had taken only limited action to encourage local authorities to develop and improve their asset management plans in line with its expectations. The Welsh Government told us that the 21st Century Schools Programme, a collaborative approach with local government, and the transitional projects leading into it are intended to clarify the definition of fitness for purpose, the Welsh Government funding envelope and to provide medium-term planning for the Welsh Government and local authorities.

- a** to clearly articulate the approach, the rationale, the benefits and risks and discuss them with those who will be involved in delivery;
- b** to be clear as to accountabilities and expectations, in particular the extent of local flexibility and central direction;
- c** to be clear about what success means and how to track progress, including the long, medium and short-term outcomes that are to be achieved and measurement of each party's contribution to achieving those outcomes over time;
- d** to put in place appropriate governance arrangements that match the chosen approach and enable risks to be managed; and
- e** to encourage an open relationship based on sharing learning about successes and difficulties in delivery in order to address problems and improve.



Despite positive examples of progress, health service transformation needs to be accelerated and the NHS is likely to struggle to meet the immediate financial challenges unless it revisits some of its ambitions

2.9 The NHS faces significant future financial challenges (see [Part 1](#)). This part of the report sets out our observations on the NHS' preparedness to face these cuts. It examines the overall direction provided across the NHS, and draws on our local work to comment on the preparations that are being made by Health Boards and NHS Trusts across Wales.

The NHS Five Year Framework rightly focuses on transformation to improve services and reduce cost but its goal of improving quality and maintaining service levels and jobs while reducing costs is highly optimistic

2.10 The Welsh Government is developing a longer-term approach to NHS planning; integrating financial, delivery and workforce planning across a five-year time frame. The June 2010 *Five Year Service, Workforce and Strategic Financial Framework* set out the three main challenges facing the NHS in Wales: poorer health outcomes for the NHS in Wales when compared with peers; inconsistent quality of service and a significant funding gap as a result of cost, demand and budget pressures. The Welsh Government has a goal of bridging the financial gap it faces at the same time as improving the quality of care and maintaining service levels and jobs.

2.11 There is no doubt that there is scope to transform NHS services to increase productivity, deliver real cost reductions and to improve service quality. The Five Year Framework's plans for reconfiguration reflect our own analysis that the NHS is over-reliant on expensive hospital care when people could get more cost-effective treatment in the community. In particular, too many people with long-term chronic conditions are treated in hospitals when they could be cared for elsewhere and supported through integrated health and social care services. The challenge is that, to save money, such reconfiguration requires not only new capacity in the community but also requires that existing capacity – including hospital beds and wards – be closed down.

2.12 As well as needing to move care out of acute hospitals, there is scope to further improve efficiency within hospitals for patients who do need to be there. Systemic and process weaknesses mean patients sometimes stay in hospital longer than clinically necessary. The NHS has made progress in some key areas, like admitting more people on the day that they are due to have surgery. And there has been an improvement in the rates of day surgery, although there is scope for further improvement. However, early findings from our work on operating theatres are revealing many examples where surgical theatre time is being under-used. Making better use of existing capacity and reducing the time people spend in hospital can improve productivity and, potentially help to deliver cash savings. Our work on the consultant contract has identified opportunities to better plan the work of consultants, to support wider service improvement and modernisation. There is also scope to reduce cost in non-clinical areas as our recent report on hospital catering demonstrated ([Figure 17](#)).

Figure 17 – Hospital catering

The NHS spends £60 million a year on providing catering services, of which £14.8 million is spent on food. We identified significant variation across the acute hospitals in Wales between the costs per day of providing patients' meals, the figures ranging from £5.99 to £17.54. It should be noted that those hospitals which spent more per day on patient catering did not have the highest levels of patient satisfaction, and so reducing costs in this area would not necessarily result in a poorer service to patients.

Reducing food wastage is another way of controlling costs. Hospitals report levels of food wastage to Welsh Health Estates, where wastage is defined as 'unserved meals'. Using this definition, we carried out our own assessment of food wastage on 62 wards across the 23 acute hospitals comprising our study. We found that on average 15 per cent of food was wasted (amounting to £1.5 million), but there was considerable variation, ranging from some wards in which no food was wasted to other wards where 62 per cent of food was wasted. We calculated that if all the health boards and trusts reduced food wastage to the level of some of the best performing wards in our study then they could have made savings of £758,000.

We also looked at the costs of providing non-patient catering services across the acute hospitals in Wales. We found that in only one of the health boards or trusts did non-patient catering services generate sufficient income to break even, in all other cases non-patient catering was subsidised. The deficit level ranged from 14 per cent to 45 per cent. It was significant that, although all but one hospital subsidised non-patient catering, none of the organisations had a specific policy for doing so. And there was limited visibility of this subsidy, with information on non-patient catering not being provided to hospitals' Boards. We estimated the value of the subsidy to be £2.5 million in 2009-10. We would suggest that in the current economic climate hospitals at least find ways to ensure that non-patient catering services break even.

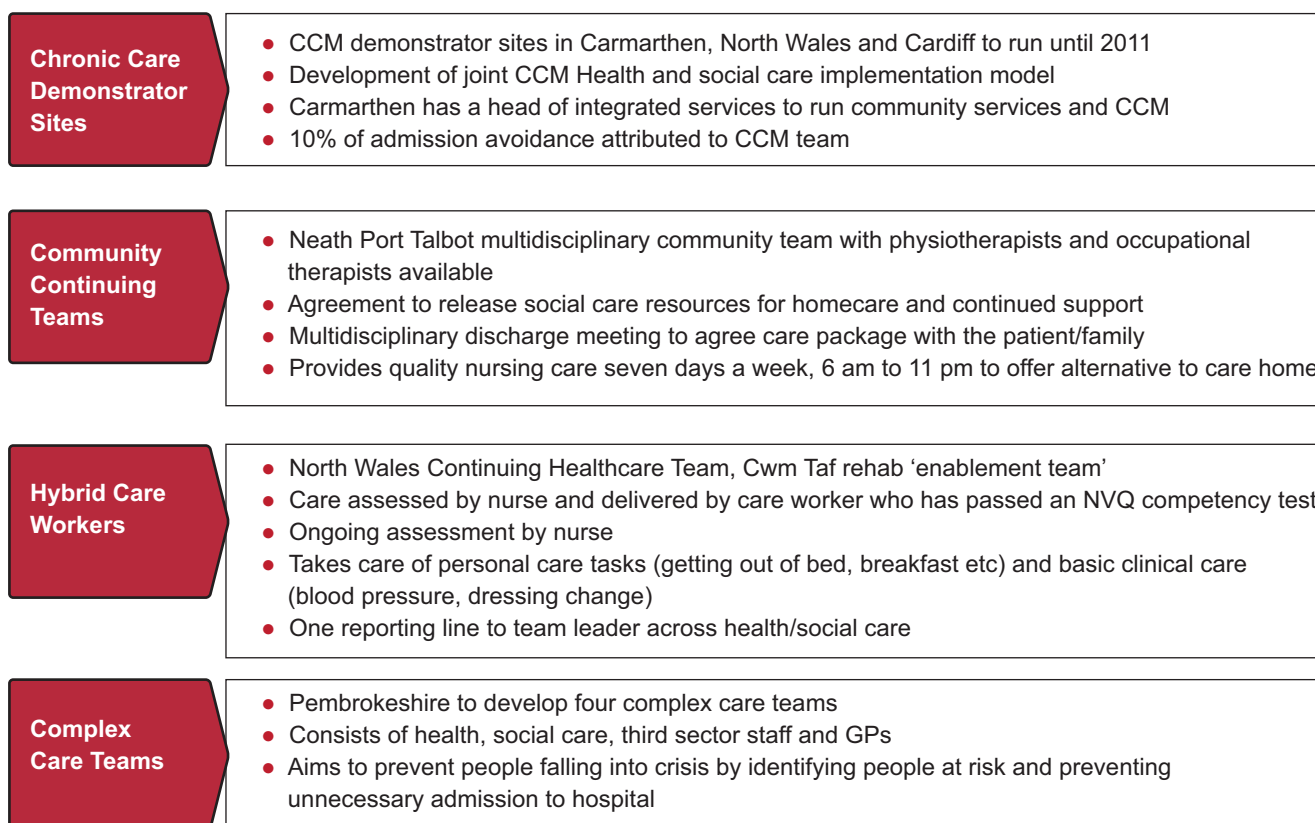
2.13 Across the NHS, there are examples of innovative ways of working to improve the efficiency and effectiveness of hospital services. For example, the 1000 Lives Campaign and its successor 1000 Lives Plus are reporting significant improvements to patient care, as well as identifying

opportunities to improve productivity and reduce costs. The approach is rooted in the lean/systems thinking method (paragraph 2.51). It provides staff working on wards with a method for understanding how the services they provide can be improved to reduce variation, harm and waste. The programme encourages staff working on the wards to take responsibility for identifying ways to improve. One of the key impacts reported by the programme, as well as saving lives and reducing incidents of harm, is that it has virtually eradicated the incidence of pressure ulcers, commonly known as bed sores, with the knock-on effect of freeing up staff time to concentrate on other elements of patient care.

2.14 The Five Year Framework's goal of bridging the funding gap while improving quality and sustaining levels of service and jobs, particularly in the short term, is highly ambitious. The NHS has struggled to deliver the kinds of reforms currently being planned, since at least 2003, when Derek Wanless reported on the Welsh NHS. There are examples of positive progress. The Five Year Framework identifies a number of demonstrator examples of elements of services that have been improved and integrated (Figure 18). The Five Year Framework sets out an 'adopt or justify' approach, requiring services to adopt the models in the demonstrators or justify why they intend not to. The Welsh Government has required all health boards and NHS trusts to produce their own Five Year Plans. However, even with the financial position and Five Year Framework adding strong impetus it is still ambitious to expect to actually deliver such reform across the NHS, and realise significant cost savings as a result, in a short period of time.



Figure 18 – Local examples of new ways of delivering services



Source: NHS Five Year Framework.

2.15 Despite the reference to sustaining levels of jobs, the number of NHS staff decreased by 293 (0.4 per cent) to 72,444, between September 2009 and September 2010. There were rises across most job categories, other than administration and estates staff, with a 15 per cent reduction in the number of managers, including a 22 per cent reduction in senior managers. It is likely that many of these managers left following the merger of Trusts and Local Health Boards in October 2009. With such a major reduction to one staff group, the scope for further cuts to

management may now be limited. And as the former Chief Executive of the NHS pointed out to the Public Accounts Committee, losing significant management capacity at a time of change is a risk which will need to be carefully managed.

Despite some positive examples, the NHS needs to accelerate the pace of progress in reconfiguring services to deliver more cost effective care and bridge the funding gaps

NHS bodies have generally done a good job of getting the mechanics of re-organisation right

2.16 The NHS in Wales faced significant re-organisation. In October 2009, the number of NHS bodies reduced from 30 to 10. We found that all of the organisations had made good progress with getting the mechanics of that major structural change right. All of the new bodies had the foundations for sound governance in place, although they all also needed to further strengthen their governance arrangements in different ways. We also found that they had done a good job of bringing together the finance systems, including financial control systems to manage and account for expenditure.

Despite some progress and positive examples, detailed local plans for reconfiguring NHS services to deliver more cost effective care are still some way from completion

2.17 Our audit work during 2010-11 found that NHS bodies were at varying stages of planning for service reconfiguration. Most were making progress in developing plans, but were at varying stages. The demonstrator sites show that there are examples of reconfiguration in individual services. However, in general, plans were still some way from completion, and some bodies were yet to clearly identify the service models they intend to adopt.

2.18 We found that while all NHS bodies were doing medium-term financial planning and some workforce planning, in general this was not comprehensive. Without clear service reconfiguration plans, NHS bodies struggle to clearly identify the future costs and potential savings. We found examples where NHS bodies had not identified how they would find the capital funding needed to develop new services. The Welsh Government has introduced an invest-to-save programme to help the NHS, and other public services, invest in changes that will lead to savings. Part of the savings will be used to pay back the investment over time, rather than bridge immediate funding gaps. We found that work to identify savings from reconfiguration was often not well developed. Inevitably, savings through reconfiguration will involve reducing staff costs. The challenge is to get that reduction right, so that staff remain engaged and skills gaps are avoided. Our work found that across the NHS, workforce planning was progressing, but that almost all NHS bodies had yet to develop plans which were fully responsive to the current financial pressures or to future service models.

2.19 In the past, the NHS has experienced problems in taking, and acting on, tough decisions to transform and re-shape services. Changes in the provision of local services, including moving some services out of hospitals and reducing or shutting some hospital services, are inevitably controversial. Following the re-organisation, managerial leadership in the NHS is more concentrated, which should help make decision making on reconfiguration more streamlined. The NHS should now use the opportunity of the new political cycle, to engage the public and communities, and move forwards with the difficult and controversial changes that are needed across Wales.



There are positive examples of partnership working, some leading to service change, and public engagement which will help support wider reconfiguration of services

- 2.20** Through our recent audit work, we found that the process of NHS reorganisation had not had a detrimental impact on local partnership arrangements, although a small number of organisations experienced early problems which have largely been addressed. With fewer NHS bodies, the re-organisation is intended to reduce complexity and support better partnership working. We found that at least four of the bodies took forward their commitment to the principle of partnership through joint appointments with local authorities, and there are many cases across Wales where collaborative working has led to shared use of buildings. We also found examples where partnership working had led to changes in the way services are delivered or planned.
- 2.21** Public engagement is also critical to the success of service transformation. It is difficult to achieve consensus around controversial decisions, particularly when closing facilities and services, such as hospitals, which are often highly valued by local communities. The tensions between service reconfiguration and the views of the public and patients are best managed through effective communication and engagement. We were encouraged therefore to see that at least four organisations had engaged the public and/or service users on plans to change services, and it is clear that organisations are embedding the use of patient experience data to improve services.

The scale of the financial challenges and the progress to date in reducing overall spending suggest that the NHS may need to reconsider its ambitions for service levels and jobs if it is to achieve financial balance in the short term

- 2.22** NHS bodies reported that they had achieved £313 million of efficiency savings across 2010-11; significantly higher than in previous years. We have not audited the claimed savings but it is unlikely that all of these are cash-releasing savings that help directly bridge the funding gap. Clearly, individual organisations have achieved transactional savings, for example, our audit work has identified positive examples of improved procurement practice. However, audit work on efficiency savings across the UK tends to show that many of the claimed savings cannot be verified.
- 2.23** Given the track record of the NHS in managing within its budget, the scale of the funding gap and with widespread service reconfiguration some way off, it is very difficult to see how the NHS will improve quality and sustain service levels and jobs in 2011-12 without again requiring a significant cash injection from the Welsh Government. However, with all Welsh Government budgets facing cuts, the scope for finding such funding at the end of the year is reduced. The danger is that if no end-of-year funding is forthcoming, the NHS may need to make short-term cuts without having the time to assess the potential impact on patient care.
- 2.24** In our view, the NHS needs to accelerate the delivery of service reconfiguration to more cost effective and sustainable models and continue to build on approaches, like 1000 Lives Plus, to improve the quality of services to the patient. But this transformational work is unlikely to be sufficient to address the short-term funding gaps. The NHS may

therefore need to revisit its ambition to sustain service levels and jobs. Detailed analysis will be required to assess the potential impact of any reductions in services or staffing levels on patients and wider community outcomes before decisions are taken. Given the scale of the short-term funding gap such planning should be an immediate priority.

Most councils are inherently well placed to address immediate funding gaps but they need to do more to manage the impact of cuts, and they are unclear about the cost, risks and benefits of transforming services through collaboration

2.25 This part of the report considers the progress being made by councils across Wales in preparing for funding cuts. It considers the preparations and planning taking place locally, drawing from our local audit work. It also looks at the national direction being set for the sector, particularly in terms of a series of reviews of the structures of local government and some of its key services which are driving an increased focus on collaboration.

Most councils are well placed to cut costs, but need to make progress with workforce planning and service change to minimise the impact of cuts on service delivery and social outcomes

2.26 In November 2010, we produced a summary of our work reviewing councils' corporate arrangements, looking in particular at what those reviews said about the preparations to deal with the budget cuts. That report concluded that while many councils are becoming reasonably well placed to respond,

almost all need to make progress with detailed financial and workforce planning to reduce costs and a few need urgent improvement in key areas. Our more recent work suggests that while councils have made progress, many of the challenges, particularly in workforce planning, remain.

2.27 As a sector, local government is relatively well placed to manage funding cuts in the short term. As we reported in **Part 1**, councils have been able to build up reserves over the years and they have a good track record of delivering within budget. Councils have also been able to bridge some of the gap by raising Council Tax levels. Local government has been quite open about the possible need for cuts, to service levels and to jobs, and they have been planning on this basis. The main challenge for local government is not its preparedness to cut costs, but its ability to minimise the impact of the cuts in terms of service delivery and wider outcomes.

2.28 Making decisions about what to cut, what to protect and where to invest in improvement requires a clear set of priorities and intended outcomes. Our work points to a mixed picture in terms of priority setting. Some councils have struggled, with several identifying most things they do as a priority, or coming up with objectives that are too broad to effectively inform decision making. However, the general trend is that councils are becoming more focused on a smaller set of clear priorities. Some have engaged well with the public and staff to set priorities in light of the financial challenge. In some cases, there have been concerted efforts to engage all councillors in setting priorities at an early stage. But many councils have not robustly linked their priorities to financial plans, and it remains unclear how they will fund some improvement activity, particularly in areas like schools modernisation, regeneration and waste.



- 2.29** Our work suggests that many councils have been focusing on reducing staff costs in response to the funding cuts. Between September 2009 and September 2010, the number of local government employees fell from 165,100 to 161,400: a reduction of 2.2 per cent. Most councils have been making progress against a range of human resources challenges. But many have not yet done detailed workforce planning to work out what skills and staff they need to meet current and future demand and to achieve their priorities and objectives. As a result, we are concerned that some councils are not effectively managing the risks that reductions in staffing pose to the quality and resilience of services and their contribution to wider social outcomes.
- 2.30** While many councils have focused on reducing costs through staffing levels in the short term, they are increasingly adopting a transformational approach. Many plan to review and re-shape services so that they can be sustained and contribute to improved outcomes, potentially with fewer staff. More and more are using, or intend to use, lean/systems thinking type approaches. We found examples where councils had managed to reduce the number of people required to deliver a service, following such reviews. Common areas of focus include housing benefits/council tax, development control (planning), and street-scene services. While there are positive indications of an increasingly transformational approach, many councils still need to make further progress to:
- a** increase the pace of change in reviewing, re-shaping and improving their services and fostering cultures to support staff in identifying and delivering new ways of working;
 - b** link service change and workforce planning, particularly redeployment and retraining, to make the best use of staff who are displaced by service reviews; and
 - c** clarify how local service transformation links to the collaboration agenda.
- 2.31** Driving through budget cuts, service transformation and greater collaboration will test political and administrative leaders in local government. There have been recent changes in senior management, with several south Wales councils appointing new Chief Executives and two of the six councils in North Wales not having a permanent Chief Executive in post. Political and administrative leaders, whether new to the job or not, are unlikely to have previously faced the challenges of delivering sustained real-terms budget cuts and change. They will need to set a clear direction and drive through change while keeping staff and local people engaged, as well as finding new ways to lead in collaboration.
- 2.32** One of the key challenges for leaders, and those scrutinising them, will be to make sure they have the information they need to manage the impact of cuts on service quality and outcomes. We have long been concerned that too much of the information councils gather measures processes and how long it takes to carry out an activity. Too little is based on the actual quality of the service provided to the service user, and the wider impact of services in improving outcomes for the communities the council serves. Councils need more meaningful information on service quality and outcomes to inform their planning and decision making, particularly decisions on where to cut and invest. They also need better information against which to measure the impact of their decisions to change services, and amend and adapt where there are unforeseen negative consequences.

Councils are responding to increasing pressure to collaborate but there are concerns about governance and accountability and uncertainty about the financial and service benefits

2.33 Local government is quite different from the NHS, in that each council is an independent democratic institution accountable to the local population. There is not a national framework for reducing costs through transforming services. However, the Welsh Government has an important role in setting the legislative, strategic and financial environment within which local government operates. There is an ongoing debate around whether local government should be reorganised, with a view that some authorities may be too small to be viable. The Welsh Government has commissioned reviews of local government structures as well as the two main council services: education and social services. Each of the reviews points to increased collaboration between councils as key to transforming services so that they are more financially sustainable:

- a** The *Local, Regional or National? What's Best Delivered Where?* review (the Simpson review) concluded that councils do not necessarily need to be reorganised, but do need to work together more across a range of services, with a mixture of arrangements to reflect local circumstances, and with some services being delivered nationally. The review challenges councils to rapidly increase the pace and scale of collaboration to deliver improved outcomes for service users and citizens, and to get better value from public spending. The review noted that the financial settlement for local government was more favourable in Wales than other

parts of the UK, and observed that the Welsh Government could rightly expect to see a return through enhanced public services. It argues for radical re-shaping of service functions, concluding that 'steady as you go is not an option'.

- b** Wales' poor showing in the international Programme for International Student Assessment (PISA) report²¹ and the weaknesses identified by Estyn²² are providing a stimulus for change in education. Following the frontline resources review²³, the Welsh Government has prioritised work to identify ways of re-directing resources to the frontline. The Welsh Local Government Association has agreed that councils will increase the proportion of budgeted expenditure on schools they hand directly to schools from the current 75 per cent to 80 per cent in two years and to 85 per cent within four years. And a review of the structure of education services²⁴ has increased the pressure on councils to work together through regional consortia to improve the cost effectiveness of school services and thereby divert resources to the classroom.
- c** *Sustainable Social Services for Wales: A Framework for Action*²⁵ sets out an intention to transform social services. It recognises the significant financial and demand pressures social services face, and aims to address those pressures through renewal, rather than retrenchment. It calls for greater collaboration between councils, with some services provided regionally and nationally, as well as better collaboration between services in the same council and local health services.

21 Bradshaw, J., Ager, R., Burge, B. and Wheater, R. (2010). *PISA 2009: Achievement of 15-year-olds in Wales*. Slough: NFER.

22 *The Annual Report of Her Majesty's Chief Inspector for Education and Training in Wales 2009-10*

23 Pricewaterhousecoopers (2010) *Review of the cost of administering the education system in Wales – Phase 1*, <http://wales.gov.uk/docs/dcells/publications/100518reviewofcostadminen.pdf>

24 <http://wales.gov.uk/docs/dcells/publications/110412educationen.pdf>

25 <http://wales.gov.uk/topics/health/publications/socialcare/guidance1/services/?lang=en>



- 2.34** Although there has been a lot of focus on collaboration, as the Simpson Review notes, there are still some significant unanswered questions about making it work in practice. Collaboration is not an end in itself; it must be for a purpose. Core to that purpose is the need to sustain and improve services and outcomes for people and communities. Given the funding challenges, financial considerations around the cost and potential cost reductions associated with collaboration are also important factors. Collaboration can take many forms, and it is not yet clear how exactly the various forms of collaboration can be made to work to deliver those key, and sometimes competing, purposes of improving services and outcomes and reducing costs.
- 2.35** One important form of collaboration is between two different types of organisation serving the same population. This kind of collaboration is essential because organisations need to work together to take a whole systems perspective and deliver seamless services that are efficient and improve outcomes for the population they jointly serve. Our work has shown that many councils are working more closely with partners in other sectors. In particular, there is increasing joint working between social services and the NHS, including joint appointments. In some cases though, councils and their partners have not set sufficiently clear intended outcomes and measures of progress to enable them to know whether they are delivering as intended. Also in some cases, the governance and funding arrangements are not sufficiently clear.
- 2.36** Councils are planning to collaborate with each other more to plan and deliver services either regionally or sub-regionally. There remains a lack of clarity as to what service and financial benefits this form of collaboration can bring, under what conditions and in what circumstances. Collaboration is not a one-way street: in a letter to the Education Minister, the Chief Inspector of Education and Training in Wales noted that complex governance arrangements for collaboration have the potential to increase costs. Those costs can be hidden, such as increased management time in making the collaboration work rather than focusing on other activity to improve services or reduce costs. There are some examples of long-standing collaboration between councils in areas like waste management. Our work suggests that such collaboration can be beneficial, particularly for specialist services, but takes a lot of time and investment in relationship management. Decision making can be slower than within a single organisation, consensus is hard to achieve, and there is a risk of solutions that represent the lowest common denominator, enabling each council to show they have got something out of the arrangement, rather than what is best for the whole region.
- 2.37** Councils are looking to for ways to increase the pace and scale of collaboration but are now having to confront some of the uncertainties and risks involved in making it work in practice. All areas have a range of projects that are being run through the four WLGA Regional Partnership Boards. The four regional education consortia are now in place and are aiming to provide regional School Improvement Services from September 2012. In most cases, the Regional Boards'

collaborative projects are still being developed and implemented, so the costs and benefits are not yet clear. In line with the Simpson Review, many are trying to develop effective governance arrangements to enhance, rather than diminish, local accountability and scrutiny of front-line services. One of the key specific challenges is to provide clarity and assurance to local councillors and citizens that they can still have a say in the way services are delivered and hold senior managers to account where they fail to deliver. Some areas are making progress in bringing together some governance structures, but in general many of the key questions around governance and accountability remain unanswered.

2.38 Overcoming the organisational, governance, and cultural barriers means that collaboration is likely to take time before it bears fruit in terms of major financial savings. Collaborative regional or sub-regional delivery of council services is therefore unlikely to play a large role in bridging the short-term funding gaps councils face. This is reflected in the fact that councils are generally focusing on making savings through transforming their own services. However, collaborative services are likely to form an important part of the longer-term transformation of service delivery.

2.39 There is also a need to be realistic about the extent to which shared back-office services will contribute to efforts to bridge immediate funding gaps. Securing savings through sharing back-office functions may seem obvious; indeed it is described in *Sustainable Social Services for Wales* as the 'bread and butter of day-to-day delivery'. Yet in practice, groups of councils have struggled to agree a viable business case for comprehensive shared back-office services. While shared back-office services may be an appropriate long-term solution, the up-front costs,

complex ICT changes, and significant organisational, cultural and operational change involved mean they are unlikely to make a major contribution to bridging councils' funding gaps over the short and possibly medium term. However, in some transactional areas like procurement there is scope to make savings through collaboration in a shorter timeframe.

Overall, police and fire and rescue services in Wales are preparing well for the challenges they face, with clear plans and a good track record of financial management and delivering transformational change

Police forces

2.40 Work we carried out jointly with the Audit Commission and Her Majesty's Inspectorate of Constabulary (HMIC) in 2010 suggested that police forces in Wales were generally ahead of the game in terms of preparing for budget cuts. They have a good track record of delivering within budgets, and their medium-term financial plans had taken account of the possibility of funding cuts before the recession. Nonetheless, they face substantially sharper real-terms cuts than other public services in Wales. Financial plans for the four forces show how they intend to bridge a funding gap by 2014-15 of around £80 million.

2.41 Our joint work, which was carried out before the Spending Review, found that although the police forces have generally been well prepared and have planned for cuts, all four forces had the scope to deliver greater cost savings. We estimated that the four police



forces and authorities in Wales could save between £24 million and £35 million. The most significant savings are to be found through changing the skills mix, with more work done by police staff and having fewer senior officers; better procurement; and reducing back-office costs.

2.42 Even if the police forces delivered all of the efficiency savings identified above, it would not be sufficient to bridge the funding gaps that they face. As part of their plans to address the funding challenges, Welsh police forces intend to make significant reductions in staff costs. A 2011 report by HMIC showed that some forces expect to see significant reductions in the number of police officers as well as police staff. They generally expect to reduce police officer numbers through natural wastage; with officers leaving at retirement age or after 30 years of service when they have full pension entitlement. Because police officers are office holders rather than employees, they cannot be made redundant in normal circumstances if they choose to stay on after 30 years. However, there are powers to require staff to retire after 30 years in the interests of the overall efficiency of the force. One of the Welsh forces has invoked these powers.

2.43 Reductions in officer and staff numbers do not necessarily mean a decline in the quality or level of service. Forces plan to manage the impact of having fewer police officers and staff by changing the way they deliver policing. Welsh police forces generally have a good track record of delivering change. We have identified examples of Welsh police forces delivering transformational change to services in order to achieve cost reductions and protect services. We found that all the forces in Wales had made good progress with programmes of change to deliver cost reductions.

2.44 We also found that the Welsh forces are making good use of collaboration and taking something of a lead across the UK. For example, to date under the Police Authorities of Wales (PAW) £10 million of pooled resources have been used to deliver policing services on a regional basis, particularly in the areas of serious and organised crime and countering extremism. The PAW has also developed an All Wales collaboration programme to both improve services and deliver financial savings; the programme includes the scientific support unit in Bridgend which is shared by three forces.

Fire and Rescue Authorities

2.45 In 2010, we published Improvement Assessment Reports on the three Welsh Fire and Rescue Authorities (FRAs). We found that the FRAs have a good track record of ensuring that services are delivered within budget, and in this respect they are on a sound footing going into a period of significant financial challenges. All three of the FRAs had delivered an underspend in 2010-11.

2.46 We also found that all three have developed a coherent approach to planning for the financial challenges ahead, although it is too early to say if these arrangements will deliver the intended cost savings and service improvements. All three have identified the scale of the cost savings required to 2013-14. They have put in place processes to deliver the identified level of cost savings and have a range of possible options to implement. The options include reducing some management posts and reducing costs through flexible deployment of staff. One FRA intends to make 'tactical' use of its reserves if its savings plans/options do not materialise. Nonetheless, there is scope for FRAs to do more to link their medium-term financial planning to their strategic priorities and workforce planning.

2.47 The FRAs have a good track record of taking difficult decisions and delivering change through innovative programmes and projects. They had already made changes to staff working patterns. All had re-shaped their work to deliver a balance between responding to emergencies and preventative work. The FRAs all have a good track record of collaboration, particularly with the police, although some work/evaluation was needed to demonstrate the impact of some partnership working. We also found that the Fire and Rescue Authorities had made good progress in engaging the public with some of the challenges they face and in identifying priorities for the future.

Public-service leaders are working together to provide direction on areas for making savings but there is a challenge to now turn the ideas into action and there is a leadership gap on short-term cuts

2.48 Our original *Picture of Public Services* report in March 2010, referred to the Efficiency and Innovation Programme (the Programme) as part of the public sector's response to the financial challenges. Since then, the Programme has developed considerably. It has brought together senior managers from across public services as well as from the voluntary and private sector, to develop a framework for responding to financial and other pressures through efficiency and innovation. The Wales Audit Office has been actively engaged with the Programme. In July 2011, the Welsh Government decided to replace the Efficiency and Innovation

Programme with a new Public Services Leadership Group. This section sets out our view of the key lessons from the Efficiency and Innovation Programme to inform the development of a pan-public-sector approach going forwards.

The Programme provided practical direction to support the vision of efficient, collaborative, citizen-focused services delivered through an engaged and involved workforce

2.49 The Programme built on the existing vision of efficient, collaborative, citizen-focused services, developed in the *Making the Connections* document in 2005, and endorsed by the Beecham Review in 2006. Our audit work over the years suggests that public services have been slow in moving towards this model in practice. There have been few stand-out examples that demonstrate what such a vision looks like and how exactly public services can move from where they are to the desired state.

2.50 The Programme started to offer greater detail on what collaborative, citizen-focused services might look like in practice and provided detailed support and guidance for actually implementing such services. There were two particularly promising strands of work:

- a** the lean/systems thinking work being undertaken by the Transforming the Business work-stream; and
- b** the collaborative models being promoted by the New Models of Service Delivery work-stream.



2.51 The lean/systems thinking work offered a practical approach to delivering staff-led, customer-focused improvement. Lean/systems thinking provides a structured method for staff to understand why their service is performing as it is and to innovate and re-design services to reduce waste and improve services and outcomes. The Transforming the Business Board and Wales Audit Office have jointly commissioned research from the Lean Enterprise Research Centre at Cardiff University, which sets out a model for 'system lean' to help public services

collaborate to improve services (Figure 19). The community of practice set up under the Board, and which is still in existence, offers an excellent opportunity for public services to move towards implementing such approaches in a supportive environment of shared learning. The Wales Audit Office, with Public Services Management Wales, led a visit involving senior managers from across the Welsh public service to RICOH in Telford, which has won awards for its approach to Lean (Figure 20).

Figure 19 – Lean Enterprise Research Centre (LERC) research on business improvement

The Wales Audit Office and Welsh Government jointly commissioned LERC to carry out a baseline review of the use of business improvement tools in Welsh public services, examine the scope for approaches such as lean and systems thinking to be used for complex and cross-cutting services, and provide a framework for making use of such approaches for different types of services.

The LERC's research found that there is widespread awareness and interest in business improvement approaches across Welsh public services. However, their use tends to focus quite narrowly on points of activity, rather than being used to address and improve whole systems. The report calls this ad hoc approach 'lean light'.

The report argues that it is possible, indeed preferable, to use lean and systems thinking as a whole systems approach to improving public services. The report calls this approach 'system lean' and sets out a framework for managers and leaders to use for different types of services. It is not intended to be prescriptive: the idea of a one-size-fits-all approach runs entirely contrary to the lean and systems thinking philosophy. Instead, it identifies a range of tools that can be used to enable public services to understand how their services are performing and why, from a customer-focused perspective, and how they can be improved. It identifies three different levels of service (see diagram below) and recognises that different analytical and improvement approaches are required for each level to work effectively. The full report sets out a range of different tools for the different levels and the different types of activities that can fall within those levels, and can be found at www.wao.gov.uk

Organisation/Supply chain/Cluster	Level 1 (Focus)	Level 2 (Flow)	Level 3 (Resilience)
Local authority	Leisure Services	Swimming visit process	Reliability of Life Guard services
Healthcare	Planned Care (Health and Social Care Provision)	Dementia Pathway	Care Bundle for Central Line Infection
Housing Association	Estate Management	Voids Management	Kitchen refurbishment
Police	Traffic Enforcement	Motorway patrol	Speeding ticket issue
University	Teaching	Undergraduate admissions	Enrolment process

Figure 20 – RICOH's employee-led approach to improvement

RICOH is a Japanese manufacturing company, with a plant in Telford, England. It uses a form of Lean to promote continuous improvement across all of its operations. Some of the key principles behind RICOH's approach are:

- the key is about changing people not just changing processes;
- it is about everyone, every day doing something better than yesterday;
- use your brains not your money to solve problems; and
- recognise and reward the behaviours you want to see, for those are the ones that will get repeated.

RICOH trains staff in specific methods to help them identify waste and opportunities for improvement. The company strongly encourages all staff to make suggestions for continuous improvement. RICOH rewards staff and teams for putting forward ideas in a number of ways: they get canteen vouchers for each idea that they put forward; there are regular events where staff get certificates for the best ideas; and staff are rewarded through the appraisal system.

Chris Nicholls, Manufacturing General Manager at RICOH's Telford Plant explains: 'I strongly believe that sustainable improvement is about changing people not processes. Our people doing the work are the real experts. Engaging them in continuous improvement activities brings real business benefits to the organisation.'

RICOH uses a simple but highly visual approach to management. The company's mission and the plant's values are displayed prominently across the site. They use a small number of key indicators related to quality, productivity, safety and continuous improvement. These management boards are found across the plants and updated in real time. This gives staff and managers an instant picture of the performance of a particular process or system, as well as a picture of how well they are improving.

RICOH reports strong impact as a result of their approach to continuous improvement:

- using standard measures of engagement among their 853 employees is 76 per cent, which compares very well with the average of 24 per cent;
- staff satisfaction with their job was even higher;
- the staff suggestion scheme, 'RPL together' has a return on investment ratio of 1:14;
- they get about 2,500 ideas generated a year and implement almost 80 per cent of them; and
- they use lots of really straightforward and simple practical tools which help people take control of their jobs, improve what they do and create and maintain engagement.



2.52 The New Models of Service Delivery work-stream identified examples of services and models that are designed and delivered around the user and citizen. Some of the work drew on methods used by the Kafka Brigade to gain an understanding of how people actually access services (Figure 21). This work-stream generally found that there is no one-size-fits-all model, even to address the same set of problems. Instead, the work-stream focused on characteristics of success. Often these characteristics involve systematically understanding the needs and experiences of service users/intended beneficiaries and then re-shaping the service to meet those needs.

Figure 21 – Kafka Brigade Method

The Kafka Brigade has developed a method for improving and re-designing services based on a deep understanding of how people really access and use public services. Like lean, it involves tracking service users as they interact with public services in an effort to get the service they want or need. It often highlights the complexity of getting a service; having to go to many different organisations and confusion about who is responsible for what. The method also involves bringing service providers face-to-face with service users, so that they can find out first-hand the difficulties and barriers people experience in getting a service.

There are three stages to the method. Stage one diagnoses the problem and uses frontline staff as experts to validate the emerging findings from the service users' experience, and as the source of potential solutions. Stage two involves 'galvanising change', including bringing together the multiple stakeholders with an interest in the problem to develop potential new ways of working which are implemented and assessed. Finally, the method focuses on delivery and following up to identify progress to date and identify and address barriers to action.

In Wales, the Kafka Brigade method has been used in relation to complex social problems, like domestic abuse or young people not in education, employment or training.

The work-streams identified a range of projects with the potential to deliver cost savings and/or improve services, mostly in the medium to long term

2.53 The work-streams developed or promoted a range of projects or products that have the potential to either reduce costs or improve services. In some cases, these involved new pieces of work, in others the focus has been on re-invigorating existing projects and programmes. There was also a programme of work to support and enable the other work-streams. This included work on:

- a** Leadership, which focused on developing the skills of managers to deal with the changes they face.
- b** Workforce issues, which contributed to the Adapt programme to support people potentially displaced as a result of changes in service delivery. It also helped facilitate a Memorandum of Understanding between the trades unions and local government, which sets out principles to help reduce the level and impact of cuts on public-sector employees.
- c** Public-sector ICT, which supported the delivery of change and new ways of working. The work-stream identified opportunities to provide clearer direction and address the fragmented nature of ICT provision across Wales. It also identified potential to help reduce costs through better procurement of ICT and through better use of ICT to support more efficient ways of working.

2.54 Some of the work-streams focused on transactional savings. For example, work on procurement focused on getting better value from the £4.3 billion public-service spending each year on buying goods and services from suppliers, through collaborative approaches. It built on the foundations laid by Value Wales, drawing on existing procurement frameworks like xchangewales (Figure 22). The programme set up a Taskforce which set out the steps that need to be taken to improve collaborative procurement across the Welsh public sector, and potentially deliver savings of up to £200 million over five years.

Figure 22 – xchangewales

xchangewales offers an electronic trading system that allows public sector organisations in Wales to purchase a range of common goods and services. The goal is that by purchasing collectively through a single system, public sector organisations can benefit from economies of scale and reduce their costs. At the same time, suppliers find it easier to transact with public services, thereby reducing their own costs. The programme aims to help every eligible public service organisation in Wales to get involved with xchangewales.

The Welsh Government reported that, as of the end of July 2011:

- eight local authorities are live and utilising the xchangewales eTrading system;
- two local authorities are in the process of implementing the system, with another four authorities in the planning phases and aiming to start implementation from autumn 2011;
- out of the remaining eight local authorities, five are either in the process of business case development or awaiting final sign-off, and three are currently not engaged; and
- seven health boards and three trusts are now live, covering all NHS organisations in Wales

2.55 There was also a programme of work looking to make better use of the land, buildings and other assets public services own. The work-stream supported a number of local, innovative projects across Wales to act as exemplars. The work-stream promoted the take-up of the pre-existing Electronic Property Information Management System (e-PIMS). The goal of e-PIMS is to develop a comprehensive map of public-sector assets across Wales, to inform decision making about sharing, and potentially selling off some land and buildings.

2.56 As well as these transactional areas, there has been progress on more transformational opportunities to reduce cost and improve services. In its first year, the group looking at new models of service delivery focused its efforts on commissioning research to identify success factors for new models in specific areas of service delivery. Some of the key messages from its research are:

- a Collaborative services to help older people live independently are contributing to improved outcomes and promise to deliver medium-term efficiency savings. The report identifies consistent characteristics that contribute to positive impact and outcomes. However, there is a need to measure impact, particularly financial impacts, and a need to share learning between organisations.
- b ‘Team around the family’ models for families with multiple and complex support needs show evidence of service improvements, but there was limited evidence on cost savings. The limited evidence points to considerable scope to save or avoid cost: Westminster Council estimated that their approach helped avoid costs of around £20,000 a year per family supported.



- c Approaches to supporting young people not in education, employment or training (NEETs) in Swansea and Wrexham were effective in reducing the level of NEETs. While the approaches would help avoid costs of around £56,000 per person supported, those financial benefits fell to the UK Government through reduced social security payments and increased tax revenues. The research suggests social impact bonds as a potential mechanism for funding activity on NEETs (Figure 23).
- d In general there is no single model of service delivery that emerges as the winner in any of the fields. The reports show that different things work in different environments. The work-stream has focused on identifying characteristics of successful approaches, rather than trying to promote one model over another.

Figure 23 – Social Impact Bonds

Social Impact Bonds (SIBs) offer a means of attracting private investment in new models of public service delivery where there is an expectation of financial savings in the long term. An SIB involves service providers being commissioned by a statutory organisation to deliver social outcomes under a 'payment by results' contract. The intervention is funded by private investors who receive a return on their investment if improved social outcomes – and the resulting savings to the public purse – are achieved. Social Impact Bonds are being piloted in the criminal justice system, as a means of funding activity to prevent re-offending; thereby avoiding the cost of keeping people in prison.

- 2.57** The projects within the Transforming the Business work-stream focused on issues and areas of transformation that have the potential to both save money and help to improve services, if they are widely taken up. Some of the key projects were:
- a *Lean and systems thinking* – which involves: developing an all-Wales framework contract with the aim of reducing the cost of consultancy services; a community of practice; academic input building on the jointly commissioned work carried out by the LERC. The work-stream drew on this research in developing a framework for supporting public services in adopting a lean approach to business transformation.
 - b *Income maximisation*, with commissioned research looking at opportunities for councils to increase income in a range of areas.
 - c *Shared services* – which involved partly funding a pilot shared services project in north Wales, and the work-stream explored options for developing guidance and toolkits to support public services in planning and delivering shared services.
 - d *New ways of working* – looking at the potential benefits of agile working, where staff are able to work more flexibly and in a range of places, not just the traditional office.
 - e *Access transformation* – which involved options for delivering more services online, where costs are significantly lower: on average, a face-to-face enquiry costs £7.40, a telephone enquiry £2.90, and a web enquiry around £0.32. It produced a good-practice guide to the top 10 areas for improving council websites so that they better enable people to get the information and services they want online.

The key challenge is to provide a clear method for delivery, particularly a framework for sharing and transferring ideas and practices across public services

2.58 The new Welsh Government intends to take forward the key transactional and transformational elements of the Efficiency and Innovation programme. The Minister for Local Government and Communities intends to establish a new Public Service Leadership Group to provide national leadership for collaboration and to drive the pace of improvement in public services in Wales. The Group will be chaired by and report directly to the Minister for Local Government and Communities, who will work with a reformed, statutory Partnership Council for Wales to provide collective political leadership and accountability.

2.59 One of the key challenges for the new Group will be to move on to implementing the ideas developed under the Efficiency and Innovation Programme. Since it was set up, the Programme has focused on transferring 'good' or 'best' practice between public services. It has made good progress in identifying good practices and approaches. But it would benefit from greater clarity around how it intends to get public services to share, learn from and adopt or adapt those practices. In particular, one of the key challenges with good practice is 'causal ambiguity' – the fact that it can be difficult to work out exactly what elements of a practice caused the improved results. Getting to the bottom of what might be transferable from

one place to another and deliver improvement requires more than simply reading a case study. It requires in-depth discussion and transfer of knowledge and ideas. While there are some communities of practice to transfer and discuss practice, in general, the networks needed for such shared learning are not in place. A 2009 academic review²⁶ of existing research on good practice transfer identified three key success factors for successful transfer of practice, which could form the principles for a more comprehensive framework:

- 1 Context:** the wider strategic and policy factors that encourage organisations to seek to learn from others. It is about the explicit direction set by policy makers and the implicit incentives on organisations and individuals to engage in transferring knowledge and practices.
- 2 Relationship characteristics:** the nature of the relationship between the participants transferring knowledge. The 2009 review concluded that networks based on high levels of reciprocity and interaction have been found to support organisational learning processes. Power, politics and leadership are key factors that impact on the effectiveness of knowledge transfer.
- 3 Recipient and source characteristics:** this includes the organisational culture, structures and systems. A culture of trust is seen to be important as well as the capacity of the organisation to absorb and adapt to learning.

²⁶ Rashman, Withers, Hartley (2009) *Organisational learning and knowledge in public service organisations: A systemic review of the literature* *International Journal of Management Reviews*, 11(4), pages 463-494.



There is a gap in collective leadership in terms of direction on short-term cost cutting

2.60 While there has been national leadership in relation to cost reduction through efficiency and innovation, there has been no clear, pan-public-service direction around setting priorities for making cuts in services and staffing, and the importance of measuring the impact of such cuts on service users, and the wider community. As well as the impact on service users and outcomes, public services also need to take account of the knock-on impact of cuts. Reducing service levels in one area can simply result in demand and costs being shifted to another part of the public service. The obvious example here is the potential for reductions in the provision of social care to result in more people needing healthcare services. In such a scenario the public does not benefit from one service saving money at the expense of another. A collaborative approach to cutting is needed to help avoid these kinds of situations. The Wales Audit Office has developed a *Cost Reduction Guide* to help support public services in making informed decisions about reducing costs, including making cuts. The model is set out in **Figure 24**, and more detail can be found on our website.

Figure 24 – Wales Audit Office model from our guide to cost reduction

