Assessing Business Cases 'a short plain English guide'

This is intended as a short guide in non technical language to help members of Treasury teams who need to assess business cases as part of their public spending control work. It is not a guide for those who need to write and develop a business case as part of a spending proposal.

The methodology complies with and draws from the Green Book on 'Appraisal in Central Government[1]' and the recommended business case methodology is the 5 Case Model already widely used in Health and familiar to other government departments. This model is in line with in the Green Book, has been recommended by the OGC and is aligned with the OGC gateway process.

1 The role of HM Treasury

All expenditure requires approval by Treasury unless Treasury has delegated this authority to the department. Typically delegated limits will be set in line with an assessment of risk so that Treasury approval is required for some of a department's projects. Proposals that exceed delegated spending limits or which involve novel or contentious proposals generally require Treasury approval, usually given on the basis of a formal Business Case (BC).

Treasury spending teams should agree with departments a process for early warning of significant new projects and for getting an overview of the whole project portfolio. Teams should also agree with departments how and when the Treasury review will be conducted so that this is part of departments' decision-making process rather than an add-on.

In reviewing a Business Case, teams will seek to make a judgement as to whether the project is affordable, in line with other objectives and value for money. In forming this judgement, teams will need to consider the balance of risks associated with the project. There should be an iterative process with the department in order to develop satisfactory proposals but it is also permitted to reject a Business Case that you believe represents a poor strategic option, is unaffordable or represents poor value for money.

In addition to deciding whether or not to approve the Business Case, teams should also determine their strategy for staying in touch with project progress, including whether there are key actions whose implementation they will need to check and whether they will require sight of a Post Implementation Review.

A checklist of questions you may need to ask is annexed to this document, along with a list of specialist contacts for further assistance. You may also like to use the checklist associated with the Office of Government Commerce 'Gateway 3 Investment decision'.

[1] The Green Book a 'Guide to Appraisal in Central Government' available on-line at [http://www.hm-treasury.gov.uk/Economic_Data_and_Tools/Greenbook/data_greenbook_index.cfm]

2. WHAT IS A BUSINESS CASE?

The business case is a management tool and is developed over time as a living document as the proposal develops. The Business Case keeps together and summarises the results of all the necessary research and analysis needed to support decision making in a transparent way. In its final form it becomes the key document of record for the proposal, also summarising objectives, the key features of implementation management and arrangements for post implementation evaluation.

Business cases can cover a wide range of types and levels of spending. Each case will be developed to reflect the type of proposal being considered. The effort departments expend on developing the proposal should be proportionate to the likely costs and benefits.

Business Case Structure

Business cases can be broken down into 5 different aspects which are interconnected but distinct (namely, the strategic, economic, financial, commercial and management aspects of the case). The business case should enable Treasury and other stakeholders to ascertain that proposals:

- are supported by a robust Case for Change – **the Strategic Case;**
- optimise Value for Money – **the Economic Case;**
- are commercially viable – **the Commercial Case;**
- are financially affordable – **the Financial Case; and,**
- can be delivered successfully – **the Management Case.**

All of these aspects are important; however, their size will vary from proposal to proposal depending upon its nature and complexity. Some less complex business cases particularly those not involving significant new procurement, new systems or new building construction may need little or nothing by way of a commercial case and require a less complex management case. These cases (explained in more detail in Section 4 of this document) will be developed as the Business Case progresses.

3 THE DEVELOPMENT OF THE BUSINESS CASE OVER TIME

The business case develops iteratively over time, often in 3 distinct stages with more detail being provided at each stage.

Stage 1 – **Strategic Outline Case** (SOC)-the scoping stage.

The purpose of the SOC is to confirm the strategic context of the proposal; to make a robust case for change; and to provide stakeholders and customers with an early indication of the proposed way forward (but not yet the preferred option), having identified and undertaken SWOT analysis (Strengths Weaknesses Opportunities Threats) on a wide range of available options, together with indicative costs. This phase maps onto OGC Gateway 1 (Business Justification).

At this stage, you might expect:

- the Strategic Case – completed in full but may be revised later;
- the Economic Case – completed to the long-list of alternative options stage, with a recommended way forward (£) and an initially recommended short-list for further examination at OBC stage;
- the Commercial Case – addresses the fundamentals of any potential Procurement and Deal;
- the Financial Case – discusses the likely affordability of the proposed Scheme; and,
- the Management Case –outlines how the project will be set up and managed,

Stage 2 - **Outline Business Case** (OBC) -the detailed planning phase.

The purpose of the OBC is to revisit the SOC in more detail and to identify a preferred option which demonstrably optimises Value for Money. It also sets out the likely Deal; demonstrates its affordability; and details the supporting Procurement Strategy, together with management arrangements for the successful rollout of the Scheme. This phase maps onto OGC Gateway 2 (Procurement Strategy).

At this stage, you might expect:

- the Strategic Case – revisited;
- the Economic Case – completed according to the Green Book;
- the Commercial Case – outlines envisaged Deal structure/s and key contractual clauses and payment mechanisms;
- the Financial Case – contains a detailed analysis of affordability and any funding gaps;
- the Management Case –develops in more detail how the scheme will be delivered with an outline of the proposed programme/project management plan and if ITC is involved in accordance with PRINCE 2 methodology.

Stage 3 - **Full Business Case** (FBC) - detailed final phase.

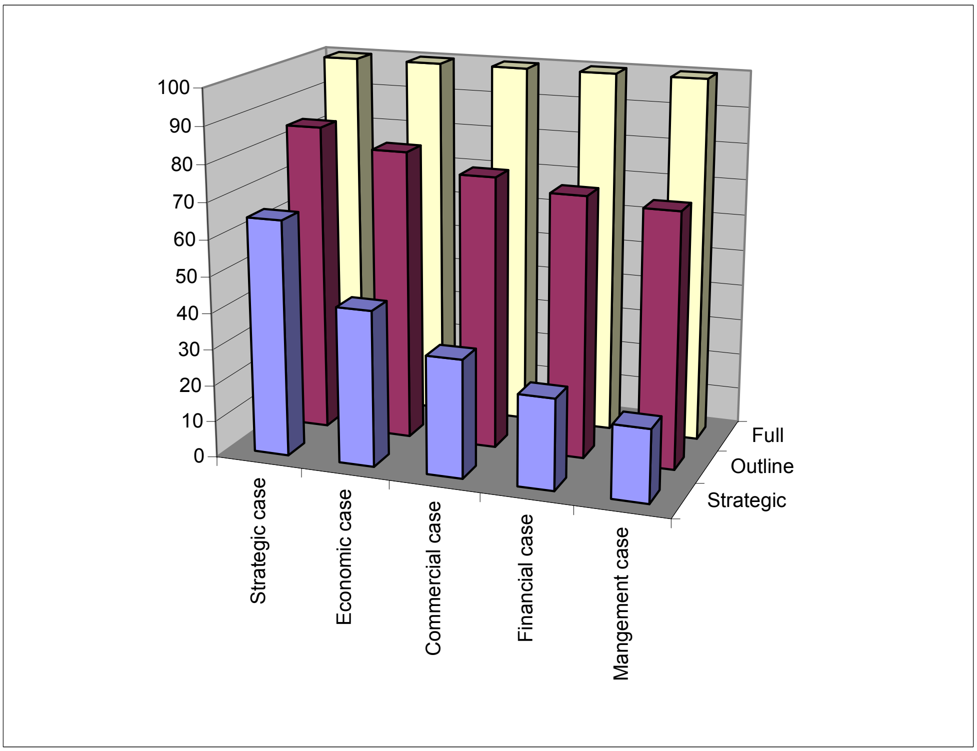
This takes place within the procurement phase of the project, following detailed negotiations with potential service providers/suppliers prior to the formal signing of contracts and the procurement of goods and services. This is usually the stage at which final Treasury approval is required.

The purpose of the FBC is to revisit the OBC and record the findings of the subsequent procurement activities; together with the recommendation for an affordable solution which continues to optimise value for money, and detailed arrangements for the successful delivery of required goods and implementation of services from the recommended supplier/s. This phase maps on OGC Gateway 3 (Investment Decision).

At this stage, you might expect:

- the Strategic Case – revisited and revised if required.
- the Economic Case –the findings of the procurement included in the analysis and recorded;
- the Commercial Case – the recommended Deal written-up;
- the Financial Case – affordability and funding issues resolved;
- the Management Case – the detailed plans for delivery and arrangements for the realisation of benefits, management of risk; and post evaluation are recorded.

The 5 aspects of the Business Case develop over time:



The spending team should retain a copy of the approved Full Business Case for their reference throughout the project

4 MORE DETAIL ON THE CONTENTS OF A BUSINESS CASE

4.1 The Strategic Case

The strategic case sets out the rationale for the proposal, it makes the case for change at a strategic level. It should set out the background to the proposal and explain the objective that is to be achieved. The strategic policy context and the fit with the wider public policy objectives and the department's corporate plan must also be satisfactorily explained, as should any interaction with or dependency on any other public sector programmes, e.g. the fit with published targets such as Public Service Agreements.

Does the strategic case clearly state the objectives which are to delivered in "SMART" terms? That is are the objectives:

- Specific,
- Measurable (delivery / achievement can be objectively Monitored),
- Achievable,
- Relevant,
- Time constrained.

If not then how is the objective clearly set out so that its achievement can be monitored? If it can not be monitored the proposal can not be judged as good value for money.

As well as the main benefits, the associated risks, constraints and dependencies of the proposal should also be considered at a high level and how they are to be managed should be outlined. Lessons learned from previous experience in this area should be briefly set out.

4.2 The Economic Case

The economic case is the essential core of the business case and should be prepared according to Treasury's **Green Book** guidance[2]. This section of the business case assesses the economic costs and benefits of the proposal to society as a whole, and spans the entire period covered by the proposal. These are not the same as the financial costs to the department or body undertaking the expenditure and an explanation of economic costs is given in the Green Book chapter 5 pages 19 to 22.

A cost benefit analysis must be performed in which the economic costs (-) and benefits (+) should be calculated for each year covered by the proposal and then summed to produce a net figure for each year. Each of these annual net values is then discounted (as set out in the Green Book) and the results are summed to give a **Net Present Value or NPV.** This NPV is the basis on which value for money is assessed, this analysis is undertaken before the decision on which option to adopt is taken.

Options Analysis

In all business cases the economic case must include a sufficiently wide consideration of alternative options for achieving the desired objective. This options analysis starts from a long list of all reasonable alternatives including a do nothing option (the so called counter factual) or if doing nothing is not possible a do minimum option.

It is important to question how the initial long list of options has been reduced to a short list of options which are then considered in more detail. Although necessarily carried out at a fairly high level, is this winnowing process of initial investigation and reasoning transparent? Reasons for exclusion might for example be obviously poor VfM or unacceptable or unmanageable risks. You may check that the potentially viable best VfM solutions are not eliminated at

[2] Ibid footnote [1]

this stage. The short list should include the do nothing or the do minimum option.

Important sources of uncertainty or risk in the proposal should be explored through the use of sensitivity analysis, under which 'switching values' should be determined and explained. These are the values at which key variables would cause the net cost benefit values to change enough to affect the choice of preferred option. For example, how much would the cost of procuring a new IT system have to rise to outweigh the expected cost-savings it will provide?

The BC should show that every effort has been made to quantify all relevant costs and benefits. Sometimes there are genuinely unquantifiable costs and benefits associated with a proposal. Where this is the case they should be clearly explained along with the reasons why quantification can not reasonably be made. Where they are relevant to the choice of option, alternative methods may be used to support option selection. It is important however that such analysis is transparent and that it is not structured in such a way as to produce a biased or predetermined result.

The BC should provide a transparent case in support of the recommended decision and artificially massaged numbers inserted to provide a predetermined result should always be rejected.

Optimism Bias and Risk

An allowance for **Optimism Bias** must also be included and provision for Risk as set out in the Green Book pages 29 to 34. In the early versions of the business case when risk management proposals are relatively undeveloped then optimism bias allowances will be higher than in latter versions when well defined risk management provisions (and their associated costs) are included. Therefore as more risk management is included and costs are firmed then optimism bias decreases.

Is the level of optimism bias included sensible in relation to the stage reached in preparing the business case and does it properly take into account the arrangements for risk management that have been built into the plan?

Have all appropriate risks been considered? Are the risk management arrangements credible, and are the risk management costs also built in?

Where PFI is involved have all the risks been examined and does the business case show that risk transfer arrangements have been agreed that move risk to the party most suited to bear it?

Distributional Impacts

Although concerned with net cost-benefit to society as a whole, where options have a different impact on different sections of society then an analysis of distributional impacts should be included and its effects explained. This should show any redistribution impact between the better off and vulnerable, disadvantaged or poorer sections of the population or even between regions of the country.

Other Wider Impacts

It is important to ensure that the proposal has considered any relevant wider issues, these will vary from proposal to proposal but the areas potentially covered include: environmental and sustainability issues; health and safety issues; consumer welfare and competition issues; rural, regional and international issues; and questions of business impact and administrative burden (Regulatory Impact Assessments). Where it is clear that the proposal has effects in these areas, the business case should set out what these effects would be and their associated costs and benefits. Where there are administrative cost impacts on the private or the third sector (or on the public sector subject to certain thresholds) an impact assessment must be included.

Rationale for choosing the preferred option

The option with the highest NPV is generally taken to be the preferred option. There may however be decisive but unquantifiable costs or benefits which although impossible to quantify are sufficient to override a simple highest VfM result. Where this is the case there must be a clear statement of these decisive factors and why they are considered sufficient to influence the decision, together with the reason for the failure to quantify them in the analysis.

The Exchequer Impact

The exchequer impact for both expenditure and taxation should be assessed separately to the NPV in the Financial Case, since the economic cost to society as a whole is blind to taxation and other transfer payments which create no additional social cost or output.

Monitoring and Evaluation

As part of their implementation all business cases should include a plan for monitoring their effects and a plan for subsequent evaluation covering when and by whom this is to be undertaken. These should include provision in both economic and financial cases for the associated monitoring and post implementation evaluation costs. This monitoring and feedback provision is essential to the longer term evolution of evidence based policy and without it the business case is not complete.

4.3 The Commercial Case

The commercial case is concerned with issues of commercial feasibility and sets out to answer the question "can the proposed solution be effectively delivered through a workable commercial deal or deals?" The first question, therefore, is what procurement does the proposal require, is it crucial to delivery and what is the procurement strategy?

The procurement strategy should be clearly set out in the commercial case and the ownership of any assets should be clearly defined and key contractual issues identified and explained, together with the proposed solution.

The allocation of risk must be clearly explained and the business case should include a risk table showing risk allocation and the steps which are being taken to mitigate risk. Any personnel implications also need to be fully explained and if TUPE is involved this has to be properly included in the delivery plans. (TUPE refers to the Transfer of Undertakings (Protection of Employment) Regulations 2006).

The commercial case should show key contractual milestones and delivery dates and should clearly set out the agreed accounting treatment.

4.4 The Financial Case

The financial case is concerned with issues of affordability, and sources of budget funding. It covers the lifespan of the scheme and all attributable costs. The case needs to demonstrate that funding has been secured and that it falls within appropriate spending and settlement limits. The focus in this section of the case is on capital and resource requirements (near-cash or non-cash) and so here VAT and capital charges are included. The financial case is concerned with the impact upon budgetary totals (RDEL, CDEL and AME as explained in Chapter 1 of the Consolidated Budgeting Guidance http://www.hm-treasury.gov.uk/

Issues in addition to the proposal's affordability are:

- does the financial case identify and fill any funding gaps,
- does it contain provision for dealing with the financing of any time or cost overruns,
- does it fully explain and estimate any contingent liabilities that may result from the proposal?

5.5 The Management Case

The management case is concerned with the deliverability of the proposal and is sometimes referred to as programme management or project management case. The management case must clearly set out management responsibilities, governance and reporting arrangements, if it does not then the business case is not yet complete. The Senior Responsible Owner should be identified.

The management case should include a delivery plan with clear milestones which relate to but are at a more detailed level than contractual milestones. The management plan applies to any programme or projects required by the proposal. Programme and project plans must include business assurance arrangements. Where so-called controlled environments such as information and communications technology are involved or complex business systems then the use of PRINCE2 methodology is mandatory for programme and project management. Where significant change management is involved, a change management and stakeholder management plan should be included.

The management plan should also set out clearly the OGC Gateway Review arrangements, and should contain a benefit realisation plan and benefit register.

The management plan should also include a contract management plan and arrangements where contracts are required. There should be a contingency plan with arrangements and plans for risk management and a risk register.

You should also consider whether the business case has been appropriately signed-off within the organisation. For example, have relevant business owners and professionals (Economists. Finance, Procurement, HR, IS, delivery professionals) approved the case?

Evaluation of the effects of the intervention after it has been implemented is a key element which is sometimes overlooked in preparation of a business case but it is vital to the evolution of evidence-based policy and must be included in all proposals. Provision for this work must form part of the management plan, with identification of who will conduct monitoring during and after implementation and who will be responsible for post implementation evaluation and when and how it will occur. There must be full inclusion of monitoring and evaluation costs within both the economic and financial cases. Without planning and provision for monitoring and post-implementation evaluation of the proposal the business case is not complete.