



Capability Review of HM Treasury

Foreword

The purpose of departmental Capability Reviews is to use honest and robust assessments of future capabilities to identify the specific measures that are needed if central government departments are to play their part in enabling the UK to meet the considerable challenges of the future.

Over the course of the last generation there has been a transformation in the UK economy and wider society. In the era of globalisation, international trends in, for example, migration, production techniques and energy consumption have a profound effect on an outwardly facing nation like the UK. Global competition places a premium on productivity and flexibility. Harnessing new technology, developing new, high-value skills and embracing change have all enabled the UK economy to respond to these challenges, but only because companies, communities and individuals have had to learn to adapt to rapid change. As the pace of change quickens, skills and flexibility will become even more important.

Just as these trends have required a major change in the behaviour of all parts of UK society – corporate, community and individual – the challenges of the future require a response from government too. If the state, through public services, is to enable the UK to thrive over the decades to come, public services and those who deliver them must also become more flexible and adaptable, more individual, more expert and more professional.

And the environment in which public services are delivered is also changing fast. Migration, an ageing population and changing lifestyles are amongst the factors that have made the UK population – the users of public services – more diverse than ever before. The nature of public services means that often the normal market-based ways in which suppliers learn what customers think of services are only partly available. But technological and lifestyle changes mean that the public's expectations are rising, as those who use services rightly demand something tailored to their needs and delivered in the way most convenient for them.

Equipping public services for these challenges requires a transformation of the nature of government. The Capability Reviews mark an important part of this process for the centre, with an examination of what the needs going forward are for each government department.

Underpinning each review is how each department can play the role of enabler. In the modern era of technological change and consumer choice, it is not for government to control or prescribe what people want and receive.

Instead, a clear vision of what the centre should do is fundamental. High-level targets are an important tool, but the centre cannot and should not seek to micro-manage everything. Instead, the centre needs strong strategic capability to set and review priorities, as well as robust systems for managing performance and tackling areas of weakness. Getting the right skills in place, particularly operational

skills, is of critical importance. Equally crucial is ensuring that policy is designed in a way that uses what works for customers and providers. These are the themes of the Capability Reviews.

Each Capability Review has been carried out by the Capability Reviews Team in the Cabinet Office, with a team of external reviewers assembled specially for the department under review. These reviewers have been drawn from the private sector, the wider public sector and board-level members of other government departments. The teams' wealth of experience provides external challenge and insight as well as contributing to sharing best practice across Whitehall.

I would like to thank and acknowledge the support of the review team for HM Treasury (HMT), without whom this report would not have been possible. The members of the team were:

- Dr Keith Burgess OBE, Chairman, EMEA, BearingPoint
- Andrew Cahn CMG, Chief Executive, UK Trade & Investment
- Helen Edwards CBE, Chief Executive, National Offender Management Service, Ministry of Justice
- Amelia Fawcett CBE, Chairman, Pensions First
- Barry Quirk CBE, Chief Executive, London Borough of Lewisham

This report is just the beginning. The real challenge for HMT comes in implementing what has been identified as needing to be done. Key actions which address the areas for improvement have been agreed between the Cabinet Secretary and the Permanent Secretary of the Department. The Capability Reviews Team will regularly review progress and provide support to help ensure that HMT is on track to deliver.



Sir Gus O'Donnell KCB
Cabinet Secretary and Head of the Home Civil Service

December 2007

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The Department's response

The Department has responded to the findings of the review and identified four areas of action. The Cabinet Secretary will use these to hold the Permanent Secretary to account on progress.

The Permanent Secretary's response

The Treasury Board and I welcome this report. The Capability Review was well timed. The UK economy continues to show remarkable stability, with 61 quarters of unbroken growth and continuing low inflation, but this autumn has seen greater economic and financial uncertainty across the main industrialised countries, and the review provides the opportunity for HM Treasury (HMT) to look again at the way in which the Department operates and to challenge embedded assumptions.

We are pleased that the review recognises that there is much that is excellent in the Department. I believe that the Department should be proud of its record and celebrate its achievements.

The review identifies important areas for action, ones which the Board and I recognise. We have already begun to address these issues and we are pleased that the review gives us credit for work already under way to strengthen our workforce and clarify roles and responsibilities at the centre of government. However, we are not complacent and know we have further to go if we are to achieve lasting cultural change in the Department.

In January 2007, the Board set out a vision for the Department. This review confirms that the Department is heading in the right direction. The workstreams of activity we have identified in response to this review give us the basis for a comprehensive plan to help us achieve our vision.

I am determined to build on the momentum created by this review to reinvigorate work already under way, to build on our strengths and address our weaknesses to become an even more successful Department.

Developing our people resource: culture and skills

We welcome that the Capability Review recognises the progress we have made in respect of people management. Our Workforce and Skills Strategy, launched in May 2006, is beginning to have an impact with people spending longer performing in post and a better focus on people management.

In terms of culture, there is much to celebrate about the strong identity that HMT has and its supportive working environment. However, we recognise that a strong internal culture has the potential to impact both positively and negatively in our dealings with our stakeholders. Our new values (collaborative, open, challenging and

appreciative) have set out a clear direction, but we accept that we have further to go to fully embed them.

On staff skills, we will:

- in three months, have brought together existing activities around the workforce into a comprehensive and strategic plan which is linked to our business planning process and objectives as part of the next stage of our Workforce and Skills Strategy; and
- strengthen our approach to developing our people, reviewing existing interventions, and within six months have launched a new talent management strategy which is based on a clear understanding of the skills HMT needs.

On culture, we will:

- model the behaviour we want to see from the top of the organisation, behaving consistently with our values and management behaviours at all times, and fostering a culture where staff feel able to challenge inappropriate behaviour;
- within six months, have aligned incentives in our recruitment, appraisal and promotion arrangements to support the behaviours and values we want to embody; and
- within 12 months, have embedded diversity into all of our workforce processes so that we can achieve an HMT which reflects, at all levels, the society it serves.

Strengthening relationships with our stakeholders

HMT works with and through other government departments and external stakeholders to achieve its objectives – effective stakeholder relationships are crucial to our success. There are many examples of extremely strong stakeholder relationships in the Department. In some areas, we are by necessity constrained in the amount we can consult and, being the holder of the public purse, there are times when we have to communicate hard messages. However, the Board and I recognise that we need to do more to strengthen our relationships with our stakeholders.

Led by the Public Services and Growth directorate, work is under way to agree a compact between the Treasury and the Cabinet Office, as central departments, and other government departments, including setting out best practice on both sides. We will continue to implement this, in consultation with other government departments, and hold ourselves to account through regular conversations with other departments.

In addition, we will:

- continue to encourage a culture of openness, consistent with HMT values, using induction and other development processes to set out best practice, with the Senior Civil Service leading by example;

- within the next six months, develop and begin to implement a coordinated stakeholder engagement strategy across the Department; and
- undertake annual surveys of stakeholder opinion, with the first survey a repeat of those stakeholders interviewed as part of this review, and commit to address issues raised within the surveys and report back to stakeholders on what we have done to improve.

Working together at the centre of government to support delivery

The Comprehensive Spending Review (CSR) 2007 sets out a reformed cross-government framework for performance management and delivery across government. The Capability Reviews Team reports that there is some uncertainty amongst departments over respective roles and responsibilities of the central departments for supporting delivery and managing performance across government.

We recognise this as an area for action and we know that we need to move quickly in this area to provide certainty to departments before the new Public Service Agreements (PSAs) come on line in April 2008.

Work is already under way to clarify respective roles and responsibilities for performance management between HMT, the Prime Minister's Delivery Unit (PMDU) and the Cabinet Office. Our joint board meeting on 13 December will be a key milestone in arriving at a clearer model of responsibilities for performance management. By April 2008, we will have consulted with departments and set out a coherent framework for performance management. But we recognise that this will not be the end of the process – the ongoing challenge for the Department will be to implement the framework effectively and have regular conversations with departments on what works and what doesn't. In 12 months' time, we will have reviewed the new arrangements with departments and set out how we will further refine our approach.

Taking responsibility for driving change

Strong, inspirational leadership is critical for achieving change in the areas set out above. We welcome the fact that the review found excellent examples of leadership in the Department; however, we recognise that we need to lead by example and set the standards from the top. We accept that there is more to do in clarifying the role of the Board and the Executive Management Group and we need to demonstrate more clearly that we are acting as a corporate team. We also recognise that we have not taken a systematic approach to managing change in the Department and that this has contributed in part to our lack of success in achieving change in the past.

To address this, we will:

- immediately put in place a programme to manage more systematically change across the Department, with managing directors taking personal responsibility for change in different areas and with strong Board oversight and direction;
- over the next six months, revitalise the senior leadership programme and engage the wider Senior Civil Service in the corporate agenda, including corporate objectives in all senior staff's personal delivery objectives;
- improve the governance structures in the Department and links between the various Board sub-committees, with new non-executive directors to provide additional external challenge to the Department by the end of April 2008; and
- challenge ourselves as board members in the corporacy of our behaviours and focus more of our time on managing across the whole Department rather than within particular directorates.

I do not underestimate the amount of time and effort that will be involved in achieving these changes, not least because success will come through achieving enduring cultural change rather than through delivering particular outputs. I have huge confidence in the people in HMT whose ability and talent have been recognised in this report. I am in no doubt that HMT staff will meet this challenge with the dynamism, energy and enthusiasm that they demonstrate daily in their work, and HMT will continue to build on its strengths as a world-class economics and finance ministry.



Nick Macpherson
Permanent Secretary to HM Treasury

December 2007

1. The Department

HM Treasury (HMT) is the UK's economics and finance ministry. Its aim is to raise the rate of sustainable growth, and achieve rising prosperity and a better quality of life, with economic and employment opportunities for all.

HM Treasury is responsible for formulating and implementing the Government's financial and economic policy, protecting the public finances and promoting economic growth domestically and internationally.

It is one of the oldest government departments, and its core functions have been relatively stable since 1945. However, over the last decade there have been a number of developments which have given the Department a more strategic role and delegated some operational responsibility to other bodies. In May 1997, operational monetary policy was transferred to the Bank of England. The creation of an independent Financial Services Authority (FSA) transferred responsibility for regulating banks, insurance companies, financial advisers and mortgages from the Bank of England and established a tripartite agreement between the Bank of England, the FSA and HMT to support financial stability. In April 2005, HM Revenue & Customs (HMRC) was created from the merger of the Inland Revenue and HM Customs and Excise. Whilst HMT leads on strategic tax decisions, HMRC is responsible for the collection of revenue.

HMT pursues its aim of promoting growth, prosperity, and economic and employment opportunities for all through eight strategic objectives:

1. Maintain a stable macroeconomic environment with low inflation and sound public finances in accordance with the Code for Fiscal Stability.
2. Increase the productivity of the economy and expand economic and employment opportunities for all.
3. Promote efficient, stable and fair financial markets, for their users and the economy.
4. Promote a fair, efficient and integrated tax and benefit system, with incentives to work, save and invest.
5. Promote UK economic prospects by pursuing increased productivity and efficiency in the European Union, international financial stability and increased global prosperity, especially protecting the most vulnerable.
6. Improve the quality and the cost-effectiveness of public services.
7. Achieve world-class standards of financial management in government.
8. Protect and improve the environment by using instruments that will deliver efficient and sustainable outcomes through evidence-based policies.

The Department is part of the Treasury Group, which comprises HMT, the Office of Government Commerce (OGC) and the Debt Management Office (DMO). HMT employs approximately 1,200 staff, making it one of the smallest departments

in Whitehall. OGC is an office of HMT, which is responsible for transforming government procurement and employs a further 300 staff. DMO is an executive agency of HMT, and is responsible for debt and cash management for the UK Government, lending to local authorities and the management of certain public sector funds. It employs some 80 staff. HMT benefits from a significant inflow of staff, with 22 per cent of staff on loan from other government departments. Over a third of the Budget, Tax and Welfare Directorate are inward loans, reflecting the policy partnership between HMT and HM Revenue & Customs.

In 2007/08 the Treasury Group had a budget of £307m, of which HMT accounts for £137m, OGC £27m and DMO £12m. The remaining £131m covers expenditure such as the Bank of England and coinage.

HMT is structured around four key themes:

1. public services and growth;
2. macroeconomic and fiscal policy;
3. international issues and financial services; and
4. budget, tax and welfare.

In each of these roles, HMT works with and through a wide range of stakeholders to achieve its objectives. Principal amongst these are the Bank of England and the FSA, international finance institutions, such as the International Monetary Fund, and other government departments. In its finance ministry role, HMT works with other government departments to maintain firm control of public spending and to improve financial management capability in government. In its economic ministry role, it works through other government departments to develop policies to advance growth in the UK, raise productivity and promote opportunity, social justice, stability and security for all, in the UK, Europe and internationally.

HMT works with the Cabinet Office to promote the effectiveness, efficiency and quality of public services. It also leads the management within government of staff in the relevant specialist groups, such as economics, accountancy, audit and social research.

The Chancellor of the Exchequer has overall responsibility for the work of the Treasury Group and the Chancellor's departments. These comprise HMRC, the Office for National Statistics, National Savings and Investments, the Government Actuary's Department and the Royal Mint.

The Treasury Board is chaired by the Permanent Secretary to the Treasury, and consists of six executive members, the Chief Executive of the OGC and three non-executive directors. The Board considers strategic issues that affect the Treasury Group. It is supported by the Group Operations, Finance and Audit Committees. HMT,

OGC and DMO have their own executive committees to deal with day-to-day management in the respective parts of the Treasury Group.

Whilst HMT is working hard to build a more cohesive Treasury Group, this Capability Review focused its attention on the core department of HMT. The review took place during a period of testing challenges to stability in the banking sector. Because of its timing, the review was not able to look in any depth at any capability issues arising.

2. Current delivery challenges

HM Treasury (HMT) has 10 Public Service Agreement (PSA) targets set out in the Spending Review of 2004. The Department is on track to achieve 7 of its 10 PSAs and has made good progress since 2004 against the rest. The Treasury Group has achieved, and in some cases is on course to exceed, its Gershon efficiency savings, relocation and headcount reduction targets. The Department has overseen a period of sustained economic growth and delivered some key structural changes to improve delivery.

HMT has 10 PSA targets set out in the Spending Review of 2004.

1. Demonstrate by 2008 progress on the Government's long-term objective of raising the trend rate of growth over the economic cycle by at least meeting the Budget 2004 projection.
2. Inflation to be kept at the target as specified in the remit sent by the Chancellor of the Exchequer to the Governor of the Bank of England (currently 2 per cent as measured by the 12-month increase in the Consumer Prices Index).
3. Over the economic cycle, maintain:
 - a. public sector net debt below 40 per cent of GDP; and
 - b. the current Budget in balance or surplus.
4. Demonstrate further progress by 2008 on the Government's long-term objective of raising the rate of UK productivity growth over the economic cycle, improving competitiveness and narrowing the gap with major industrial competitors. (Joint PSA with the Department for Business, Enterprise and Regulatory Reform.)
5. As part of the wider objective of full employment in every region, over the three years to spring 2008, and taking account of the economic cycle, demonstrate progress on increasing the employment rate. (Joint PSA with the Department for Work and Pensions.)
6. Make sustainable improvements in the economic performance of all English regions by 2008, and over the long term reduce the persistent gap in growth rates between the regions, demonstrating progress by 2006. (Joint PSA with Communities and Local Government and the Department for Business, Enterprise and Regulatory Reform.)
7. Halve the number of children in relative low-income households between 1998/99 and 2010/11, on the way to eradicating child poverty by 2020. (Joint PSA with the Department for Work and Pensions.)
8. Promote increased global prosperity and social justice by:
 - a. working to increase the number of countries successfully participating in the global economy on the basis of a system of internationally agreed and monitored codes and standards;
 - b. ensuring that 90 per cent of all eligible heavily indebted poor countries committed to poverty reduction that have reached 'decision point' by the end of 2005 receive irrevocable debt relief by the end of 2008 and that international partners are working effectively with poor countries to make progress towards the United Nations 2015 Millennium Development Goals (joint PSA with the Department for International Development); and

- c. working with our European Union partners to achieve structural reform in Europe, demonstrating progress towards the Lisbon Goals by 2008.
9. Improve public services by working with departments to help them meet their:
 - a. PSA targets (joint PSA with the Cabinet Office); and
 - b. efficiency targets amounting to £20bn a year by 2007/08, consistently with the fiscal rules.
10. Deliver a further £3bn saving by 2007/08 in central government civil procurement, through improvements in the success rate of programmes and projects and through other commercial initiatives.

Following the Comprehensive Spending Review (CSR) 2007, HMT is about to embark on a new set of Departmental Strategic Objectives for the period 2008–2011 that contribute to new cross-government PSAs. The Departmental Strategic Objectives are:

- maintaining sound public finances; and
- ensuring high, sustainable levels of economic growth and prosperity for all.

In addition, the Treasury Group will be a delivery partner with other government departments for seven of the new PSAs. These are:

1. halve the number of children in poverty by 2010/11, on the way to eradicating child poverty by 2020;
2. deliver the conditions for business success in the UK;
3. raise the productivity of the UK economy;
4. improve the economic performance of all English regions and reduce the gap in economic growth rates between regions;
5. maximise employment opportunity for all;
6. lead the global effort to avoid dangerous climate change; and
7. reduce poverty in poorer countries through quicker progress towards the United Nations 2015 Millennium Development Goals.

The Department is on track to achieve 7 of its 10 PSAs and has made good progress since 2004 against the rest.

- The Government continues to deliver sound and sustainable public finances, meeting both the golden rule of only borrowing to invest and the sustainable investment rule of public sector net debt, as a proportion of GDP, to be held over the economic cycle at a stable and prudent level.
- Inflation remains near the target of 2 per cent, and independent forecasters expect it to remain so over the next five years.
- International comparisons of productivity have shown that the UK is making real progress towards narrowing the productivity gap with France and the US, and that it has closed the gap with Germany.

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- Employment in the UK is at its highest level since comparable figures began in 1971.
 - Regional data shows that all English regions grew economically in 2004 and 2005 and that the poorer-performing regions narrowed the gap in growth rates with London, the South East and East in 2005.
 - HMT, together with the Cabinet Office, is broadly on course to improve public services with 78 per cent of the PSA targets set in 2004 on target to be achieved. The efficiency targets have been achieved.
 - Excellent progress has been made on improving value for money by OGC, which, through better procurement by government departments, has already exceeded its target for delivering £3bn of procurement value for money gains.

Whilst good progress has been made, there is further to go:

- Although progress has been made in some areas on to achieve the 2015 Millennium Development Goals, for example on income poverty in Asia and primary education in North Africa, the global rate of progress remains too slow and uneven, and in some cases countries are off track.
- In opening up new markets to competition, modernising the European Community's competition rules and promoting better regulation in the European Union, the risk that Europe will fail to realise the strategic ambitions of the Lisbon strategy remains significant.
- In moving towards halving child poverty by 2010, since 1998/99 the number of children in households with relative low income has fallen by 600,000. However, between 2004/05 and 2005/06, there was a small increase which increases the level of challenge.

The Treasury Group has achieved, and in some cases is on course to exceed, its Gershon efficiency savings relocation and headcount reduction targets.

By 30 September 2007, the Treasury Group has:

- achieved £18.9m annual efficiency savings, against a target of £18.7m by 31 March 2008;
- already achieved its headcount reduction target of 150 staff by 31 March 2008;
- relocated 37 posts out of London against a target of 26.5 posts by 31 March 2008.

The Department has overseen a period of sustained economic growth and delivered some key structural changes to improve delivery.

- The Government's macroeconomic framework has continued to deliver an unprecedented period of stability, with low inflation and sustained economic growth.
- The UK economy has seen 61 consecutive quarters of growth, which represents the longest unbroken expansion of any G7 economy in post-war history, and greater stability and stronger GDP growth than most of its major competitors.
- HMT has been the architect and agent of some of the key structural changes in government over the last 10 years, including:
 - granting operational independence to the Bank of England to set interest rates;
 - creating the FSA as a single statutory regulator for financial services;
 - creating HMRC to achieve more effective tax administration and tax policy development;
 - creating DMO;
 - making the statistical system, including the Office for National Statistics, independent from government; and
 - developing a new framework for government procurement by restructuring OGC.
- HMT has been involved in refining policy across Whitehall through independent reviews on a wide range of cross-cutting subjects with an economic impact, including housing, planning, skills, transport and aviation, regulation and corporate governance, and the economics of climate change. These reviews have helped to advance the contribution of economics to government policy and have produced a strong evidence base to support the work of other government departments.

3. Challenges for future delivery

HM Treasury (HMT) must be ready to address key changes and uncertainties in the wider external environment and to respond flexibly and robustly to the strategic challenges ahead. The Department must drive continuous improvement in public services and maintain macroeconomic stability. The Department must also utilise its position at the centre of government to support others to deliver. The Department is facing a challenging reduction in its own budget and is restructuring its operational support.

HMT must be ready to address key changes and uncertainties in the wider external environment and to respond flexibly and robustly to the strategic challenges ahead.

As a result of the recent disruption in global financial markets, economic prospects have become more uncertain. HMT needs to be prepared to respond to uncertainties in the external environment, and it faces the immediate challenge of maintaining confidence in the financial markets. The Department must assure itself that it has the capacity to identify future risks and that it has the resilience to deal with them.

The Department's report, *Long-term Challenges and Opportunities in the 2007 Comprehensive Spending Review*, published in November 2006, examines key long-term trends and challenges that will shape the next decade. HMT will need to respond flexibly and robustly to the following strategic challenges:

- demographic and socio-economic change, with rapid increases in the old-age dependency ratio on the horizon and rising consumer expectations of public services;
- the intensification of cross-border economic competition, with new opportunities for growth, as the balance of international economic activity shifts towards emerging markets such as China and India;
- the rapid pace of innovation and technological diffusion, which will continue to transform the way people live and open up of new ways of delivering public services;
- continued global uncertainty, with ongoing threats of international terrorism and conflict and the continued imperative to tackle global poverty; and
- increasing pressures on our natural resources and global climate, requiring action by governments, businesses and individuals to maintain prosperity and improve environmental care.

The Department must drive continuous improvement in public services and maintain macroeconomic stability.

Maintaining robust control of public finances in the face of multiple demands from across government and the public sector will continue to be one of the

Department's key delivery challenges. HMT must maintain sound public finances and adhere to the Government's fiscal rules whereby, over the economic cycle, the Government will borrow only to invest and not to fund current spending; and net public debt, as a proportion of GDP, will be held over the economic cycle at a stable and prudent level.

The CSR 2007 period, which covers government departments' budgets for the period 2008/09–2010/11, will see current spending fall as a share of GDP from 39.1 per cent in 2007/08 to 38.3 per cent by 2011/12. This commitment to a slowdown in growth of government spending means that HMT will need to place even greater emphasis on controlling public spending over the CSR period whilst working with other departments to ensure that public services continue to improve.

Alongside this, HMT needs to play a vigilant role in mitigating fiscal risks by maintaining tax sustainability, monitoring economic performance and working in partnership with the Bank of England to ensure ongoing macroeconomic stability.

The Department must also utilise its position at the centre of government to support others to deliver.

As a central department alongside the Cabinet Office, HMT supports other government departments to deliver. The Treasury and the Cabinet Office will need to work increasingly effectively together to ensure that, through effective control of finances and transformation of the Civil Service, departments are able to deliver better outcomes with less resource by focusing on greater value for money.

The CSR 2007 launched a new strategy for transforming public services over the decade ahead, to drive forward the next stage of reform and embed value for money across government. The Department has a key role to play in ensuring delivery across a new range of cross-cutting PSAs that reflect more clearly the Government's priority objectives.

The Department is facing a challenging reduction in its own budget and is restructuring its operational support.

HMT's settlement as part of the CSR 2007, announced in the 2006 Budget, set a challenging target for the Department: to reduce its budget by 5 per cent in real terms each year from 2007/08 to 2010/11. This will be achieved through rationalisation of its estate and headcount savings.

The Department will need to balance the requirement for greater flexibility and efficiency with the need to maintain and sustain an appropriate depth and breadth of experience, expertise and skills to respond to the impact of greater uncertainty and potential system shocks.

The Treasury Group is in the process of implementing an ambitious change programme for its corporate services functions. The establishment of new group shared services will realise economies of integration and scale from sharing corporate services such as HR, finance and procurement, ICT and estates management amongst the members of the Treasury Group.

4. Assessment of capability for future delivery

- The Department's capability for future delivery was assessed as 'strong' or 'well placed' in 4 of the 10 elements in the model of capability. These were 'base choices on evidence', 'set direction', 'focus on outcomes' and 'plan, resource and prioritise'.
- Four elements were assessed as a 'development area'. These were 'ignite passion, pace and drive', 'take responsibility for leading delivery and change', 'develop clear roles, responsibilities and delivery model(s)' and 'manage performance'
- Two elements were assessed as an 'urgent development area'. These were 'build capability' and 'build common purpose'.
- There were no areas of 'serious concerns'.

Leadership

L1	Set direction		Well placed
L2	Ignite passion, pace and drive		Development area
L3	Take responsibility for leading delivery and change		Development area
L4	Build capability		Urgent development area

Strategy

S1	Focus on outcomes		Well placed
S2	Base choices on evidence		Strong
S3	Build common purpose		Urgent development area

Delivery

D1	Plan, resource and prioritise		Well placed
D2	Develop clear roles, responsibilities and delivery model(s)		Development area
D3	Manage performance		Development area

The model of capability is shown at Annex A.
The assessment categories are shown at Annex B.

5. Capability Review findings

Leadership

The Department's senior leadership team has a clear understanding of its future challenges and a strong vision for the future. The Department attracts high-calibre, talented and motivated people who demonstrate pride and excellence in their work. The Department is working to improve the skills, expertise and overall professionalism of its workforce. The Board and Executive Management Group (EMG) have underestimated the drive, stamina and commitment needed to change the culture, behaviours and diversity of the Department and to secure the skills needed for the future. The Department is not driving change with sufficient passion and pace.

The Department's senior leadership team has a clear understanding of its future challenges and a strong vision for the future.

- The Board has a clear and coherent vision of its position at the heart of government and a good appreciation of its future challenges. HMT has set out new core Treasury values (challenging, appreciative, collaborative and open) to place a greater focus on how staff interact with each other and with external stakeholders.
- The Permanent Secretary is highly regarded by staff and stakeholders as an effective, credible and engaging leader. Since his appointment in 2005, he has restructured the Department and pursued a programme of change to equip it for its future challenges.
- The Permanent Secretary has strengthened the governance of the Treasury Group and has made new appointments to the Board. A new chief executive has been appointed to OGC to lead a programme of change and to transform government procurement.
- International finance institutions and stakeholders regard HMT highly, and some consider it to be one of the best finance and economic ministries in the world.

The Department attracts high-calibre, talented and motivated people who demonstrate pride and excellence in their work.

- The Department attracts talented and committed individuals who are given scope and authority to develop, often in a fast-paced environment. Staff value the non-hierarchical structure and talk positively about a climate of challenge, openness and trust, and their sense of personal job accomplishment.
- Stakeholders universally praise the Department's staff for their analytical skills and strong intellectual capacity, and these are deployed effectively to lead and contribute to policy development, in the UK and internationally.
- Staff have a strong sense of purpose, and there is both pride and a sense of prestige in their work. Of the Senior Civil Service (SCS), 80 per cent (some 10 per cent above the Civil Service average) feel a strong sense of belonging to the Department.

The Department is working to improve the skills, expertise and overall professionalism of its workforce.

- An ambitious workforce and skills strategy was launched in 2006 to improve the skills, expertise and overall professionalism of HMT's workforce and improve its approach to people management. It aims to address the impact on experience and expertise from a very high level of internal staff turnover. 50 per cent of staff at team leader (deputy director) level and just below have been in their current post for one year or less, and 50 per cent of all staff have less than three years' service in the Department.
- The Department recognises that it will need sufficient breadth and depth of experience to respond adequately to the challenges of the future.
- The Department has rolled out a new competency framework, expected people management behaviours, weighted management objectives, improved management training, career reviews and a career deal for staff with new allowances to reflect excellent performance.
- Early evaluation shows some progress over the past year in increasing the time spent in post, and the Department is now considering how to refresh and revise the strategy to ensure that it keeps pace with future challenges.

The Board and EMG have underestimated the drive, stamina and commitment needed to change the culture, behaviours and diversity of the Department and to secure the skills needed for the future.

- The Department has a well-articulated workforce and skills strategy, but there is no clear recruitment, retention and development plan to address future skills needs, improve diversity and fully embed behavioural change.
- Talent development and succession planning are seen by many as insufficiently focused and structured. HMT is not doing enough to develop the skills needed for effective stakeholder engagement or partnership building, nor is it increasing the general understanding of delivery or reinforcing the vision of effective leadership for the future.
- Whilst the Board and EMG recognise the benefits of change, they are not yet leading strongly enough to change the prevailing culture of the organisation. Staff do not believe that the Board and the Department's SCS consistently model the desired management behaviours. A recent survey reveals that only 28 per cent of the Department's SCS believes that the top team models a culture of effective teamwork.
- The same survey notes that 37 per cent of the Department's SCS believes that there is a fair system of career progression, and the most recent staff survey confirms that confidence in the system of promotion is declining. Whilst some recent senior appointments signal a new approach, staff are yet to be convinced that they need to uphold the people management behaviours and organisational values and to stay in post longer in order to achieve promotion.
- Whilst the strong culture has many positive virtues, some stakeholders and government departments believe that HMT would improve outcomes if it acted with greater humility and in a more open and inclusive way.

The Department is not driving change with sufficient passion and pace.

- Whilst there is a high regard for the Permanent Secretary, there is less confidence in the senior leadership team's experience and visibility. Staff see the Board as doing an adequate rather than a good job.
- The Department's own 2007 board review confirmed that amongst staff there is an issue regarding clarity about the purpose of the Board. It is not seen as the key leadership, delivery and decision-making body and some, both within and outside the organisation, query its effectiveness.
- The Department's SCS is uncertain of the way forward, the role it should play and the responsibilities it should have in managing change. It does not believe that the strands of the change programme have been linked together systematically to ensure buy-in and implementation.
- In its self-assessment, the Department's SCS sees itself as an effective and confident leadership cadre in marked contrast to staff assessment of the Department's SCS leadership. Similarly, the Department's SCS believes that change is well managed and is moving with sufficient pace – a sharp contrast to the views of staff, who are significantly less positive.

Strategy

The Department has strong policy, analytical and forecasting capability, which informs the Government's financial and economic policies effectively. HMT has played a leading role in developing a new framework for managing the Government's priorities. The Department is inconsistent in its approach to stakeholder engagement and building common purpose to achieve better outcomes.

The Department has strong policy, analytical and forecasting capability, which informs the Government's financial and economic policies effectively.

- The Department has earned a strong reputation with stakeholders for its strength of analysis and forecasting, and is highly regarded by its international peers.
- The Department's approach to commissioning and supporting independent policy studies to move difficult and complex issues forward has been widely commended. *The Stern Review on the Economics of Climate Change* (2006), for example, has changed the terms of debate by significantly enhancing the evidence base and elevating climate change on the international political agenda.
- The Department recognises the need to harness, retain and share knowledge in a professional services organisation. There is an evolving approach to knowledge management, and the Permanent Secretary is its champion in the Department.

HMT has played a leading role in developing a new framework for managing the Government's priorities.

- The Department led on improving the government performance framework with 30 new cross-cutting PSAs. These set out the key priority outcomes that the Government wants to achieve in the next spending round (2008–2011).
- The Department is commended by a wide range of stakeholders and government departments for consistently delivering high-quality, complex and demanding strategy positions as part of the regular Budget and CSR processes.
- The Department's strategic approach to international and regulatory issues is also highly regarded, and it is world renowned for effectively delivering UK objectives through the international finance institutions.
- A policy partnership has been established between the Department and HM Revenue & Customs to improve the interface between tax policy and delivery and to embed continuous improvement.
- The Department and the Cabinet Office are jointly developing a compact, setting out how the centre of government and departments will work together in partnership.

The Department is inconsistent in its approach to stakeholder engagement and building common purpose to achieve better outcomes.

- Whilst the Department has effective and valued relationships with some of its stakeholders in the UK and abroad, other stakeholders and government departments believe that HMT could be more effective at building trust and productive relationships.
- The EMG recognises that it needs to do more to work effectively with key external contacts by changing behaviours and perceptions and by developing a better strategic and more consistent approach to client management and engagement across the Department's sphere of influence. This needs to be worked at urgently if the Department is to be equipped for the challenges it faces.
- Some stakeholders and government departments are looking for a clearer framework for consultation. Whilst they understand the proper constraints of formal consultation in areas such as tax policy and financial services, there is scope for improved dialogue in other areas.
- Stakeholders and government departments believe that HMT is over-reliant on some individuals who, through shortness of time in post, have less depth of experience. The Department has to reconcile its monitoring role with the need to build productive partnerships, and develop ownership and commitment to HMT's agenda.
- Other government departments' finance directors, in particular, are looking for greater collaboration and support in capability building, joint problem solving and sharing best practice.

Delivery

Improvements are being made to business planning and performance management across the Treasury Group. The Department has successfully strengthened financial management capabilities in-house and across government. There is more to do to improve the internal operating framework to ensure effective delivery. The Department needs to clarify roles and responsibilities to support delivery across government.

Improvements are being made to business planning and performance management across the Treasury Group.

- In response to CSR 2007, the Department is reshaping its business planning processes to improve prioritisation, resource allocation and the oversight of delivery of the Departmental Strategic Objectives. The plan makes clear who is responsible for delivery, the risks to delivery and how they will be mitigated, and sets out the resources underpinning the work.
- Whilst it is early days, the Board has improved its oversight of the Department's financial resources, HR and performance management through a new balanced scorecard and key performance indicators.
- HMT has embarked on an ambitious programme of shared corporate services across the Treasury Group, with the aim of reducing spending on these areas by 20 per cent. Six zero-based reviews to deliver value for money have been completed and these are expected to contribute significant savings over the CSR period.
- The Department is flexible and creative in the deployment of staff to meet changing priorities and respond to emerging risks and issues.

The Department has successfully strengthened financial management capabilities in-house and across government.

- The Department has been successful in leading a programme to improve financial management capability amongst senior managers and those aspiring to senior grades across the Civil Service. This includes launching an accelerated training programme with the Chartered Institute of Public Finance and Accountancy and a finance option for Fast Streamers studying for professional finance qualifications.
- Whilst the Financial Management Review Update (2006) for the Treasury Group recognises that there is more to do to improve links between targets, performance goals, risks and financial budgets, it records overall good performance and progress.
- There is generally a positive culture of continuous improvement in financial management and governance in the Department, which should ensure that it meets its own best practice standards.

There is more to do to improve the internal operating framework to ensure effective delivery.

- In some parts of the organisation, there is an emphasis on intellectual informality and debate rather than on process, structure and frameworks, whilst in others there is greater clarity and control. Whilst the Department's innovation, flexibility and informality can be strengths, the absence of clear management in some areas to ensure greater coherence and consistency with the Department's interventions is an ongoing concern.
- When considering change, there should be more organisational discipline and a robust programme and project approach focused on outcomes to ensure that the intent for change is turned into reality.
- Whilst a new spending control improvement project is being developed to clarify the role and ways of working of HMT's spending teams, departments are looking for clarity around the relationship of spending teams with the recently transferred Prime Minister's Delivery Unit.
- The relationship between the Board and the management of the wider Treasury Group is not always clear. Some of the more delivery-oriented arm's length bodies would like to see a clearer operating framework, and more commercial awareness and delivery experience in HMT.

The Department needs to clarify roles and responsibilities to support delivery across government.

- Whilst HMT recognises the importance of working closely with the Cabinet Office to lever improvements in Civil Service capability and overall delivery, departments are looking for clearer communication and consultation on their respective future roles at the centre of government.
- Other government departments and stakeholders are particularly unclear about HMT's role in securing better value for money in other government departments and how this will operate in practice.
- Many departments believe that HMT's interactions with them are framed by an emphasis on policy development over strategic financial management. They see a tendency towards micro-management of budgets rather than a collective focus on improving strategic outcomes. Finance managers, in particular, are looking for a more supportive relationship.
- Whilst internal risk management practices within HMT have been strengthened with improved board oversight and reporting arrangements and a non-executive director chairing the audit committee, there is less clarity about the way HMT considers and manages risk across the delivery chain.

6. Key areas for action

HMT has many strengths and a clear vision for the future. The Capability Review identified four key areas for action to enable the Department to respond effectively to its future challenges and turn its vision into a reality.

Area for action 1 – work more effectively to change the culture, behaviours and diversity of the Department and secure the skills needed to meet future challenges

- HMT needs quickly to develop and implement an active and forward-thinking approach to securing the skills needed to meet its future challenges. It also should assess its resilience against future system shocks and identify contingencies.
- The Department should develop a much clearer approach to recruitment and retention and refresh its plans to improve diversity, particularly of backgrounds and experiences.
- The Department should revisit its approach to talent management and introduce a more structured approach to ensure that there is sufficient emphasis on developing engagement skills, partnership-building skills and stakeholder-management skills, and on embedding management behaviour. Working with staff and other departments, the Department should develop clear proposals for strengthening its understanding of delivery.
- The Department needs to take early steps to tackle what is perceived by many to be a pressing need for greater inclusiveness and humility in its dealings with others. The senior leadership team should model and reinforce, at every opportunity, the agreed values and people management behaviours and be seen to tackle people at all levels when these are not upheld.
- HMT should address staff concerns about fair career progression and deal with the continuing perception that extremely rapid progression through posts, with policy excellence and individualism, are valued over knowledge and experience, management competency and teamwork.
- The Department should build on and reinforce its developing knowledge management with greater sharing of skills, innovation and learning across the Department.

Area for action 2 – engage and communicate more effectively with stakeholders and other government departments to build common purpose

- The Department needs a clearer and more formal approach to stakeholder engagement and management and should construct a more open and consultative environment that listens and responds to stakeholder concerns. HMT should consider a more structured and regular assessment of its reputation amongst its principal stakeholders.
- HMT should work with other government departments to refresh its approach to how it monitors public spending whilst seeking jointly to improve performance.

- Departments in particular are looking for more interfaces at senior levels to help build capacity, improve joint problem solving and resolve issues.
- The Department should build on the strengths of its effective internal communications and press office to develop a more modern and open approach to public relations.

Area for action 3 – clarify the Department's role at the centre of government to improve performance management and support delivery across the Civil Service

- The Department should be clearer about how it will use its position at the centre of government and the new PSA framework to improve other government departments' focus on outcomes and their efficient and effective delivery.
- HMT should clarify the overall performance management framework for government and then work with departments to implement it in a consistent and risk-based way.
- HMT should work together with the Cabinet Office to become an exemplar of joined-up government. Amongst other things, it should use a new performance framework to inform permanent secretaries' appraisals and work collaboratively on building Civil Service capability.
- The Department should ensure that processes and systems are in place and adequately managed to improve the focus and consistency of outward-facing teams.

Area for action 4 – focus on the role of the leadership in driving change with pace in a new operational framework

- HMT needs to strengthen its systems and processes that support performance management, ensure consistency and control risk whilst retaining the creativity and innovation that is important to many aspects of its work.
- HMT needs to clarify the roles of the Board and the EMG and communicate them to staff to give them a greater understanding of and confidence in the leadership of the Department.
- The Board and the EMG should take this opportunity to become a more visible leadership that reinforces the vision and values and what they mean for staff. They should also model a culture of effective teamwork.
- The Board and the EMG should be more effective in driving the pace of change. Change needs to be managed in a more coordinated and structured way, with clearer governance and accountabilities. The pace and progress of change should be an integral part of the Board's review of business and monitored against clear outcome-focused milestones.
- The Board should assure itself that it is supported by non-executive directors with the right range of skills and experience to assist HMT in addressing its future challenges.

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- The wider SCS should recognise its role in delivering cultural change by role-modelling the desired behaviours and values necessary for working in this new environment.
 - The Department should look more strategically at the development needs of the SCS and address any complacency amongst the SCS about its leadership and management skills. The Department should ensure that challenging leadership objectives are included in all personal work plans and regularly reviewed and acted upon.
 - The Department should consider specific schemes to develop leaders who can deal comfortably with the challenge of both monitoring and supporting other government departments.

Annex A: The model of capability



The model of capability has been designed specifically for the Capability Reviews. It was developed through consultation with senior leaders in Whitehall and external experts. The model is deliberately selective and designed to focus on the most crucial areas of capability – leadership, strategy and delivery.

The reviews provide an assessment of capability for departments, identify key areas for improvement and set out key actions to address these areas.

The scope of the reviews is to assess the capability of departments' senior leadership in the areas above, using the model of capability. The model enables judgements to be made against 10 elements across leadership, strategy and delivery, using an underlying group of 39 questions.

Each review has been carried out by the Capability Reviews Team with a team of external reviewers assembled specially for the department under review. These reviewers have been drawn from the private sector, the wider public sector and board-level members of other government departments.

The Capability Reviews Team will regularly review progress and provide support to help ensure that the department is on track to deliver.

Leadership

Key questions that test current capability

L1 Set direction

- Do you have a clear, compelling and coherent vision for the future?
- How do you take tough decisions, and do you follow them through?
- How do you generate common ownership of the vision with your political leadership, the board, the organisation and delivery partners?
- How do you keep the vision up to date, seizing opportunities when circumstances change?

L2 Ignite passion, pace and drive

- Are you visible, outward-looking role models, communicating effectively and inspiring the respect, trust, loyalty and confidence of staff and stakeholders?
- Do you display integrity, confidence and self-awareness in your engagement with staff and stakeholders, actively encouraging, listening to and acting on feedback?
- Do you display passion about achieving ambitious results for customers, focusing on impact, celebrating achievement and challenging the organisation to improve?
- How do you create and sustain a unifying culture and set of values/behaviours which promote energy, enthusiasm and pride in the organisation and its vision?

L3 Take responsibility for leading delivery and change

- How do you role-model an effective corporate culture of teamwork at board level, including making effective use of non-executive directors?
- Do you and the senior leadership team accept the pressing need for change, demonstrate your personal commitment to it and act as an effective guiding coalition?
- How do you initiate and drive work across boundaries to achieve delivery outcomes?
- How do you manage change effectively, addressing and overcoming resistance when it occurs?

L4 Build capability

- How do you identify and nurture talent and grow experience in individuals and teams?
- Do you have the right skills across the organisation to deliver the vision? Do you have a workforce development strategy to get the best from everyone and plan effectively for succession in key posts?
- How do you manage the performance of everyone transparently and consistently, rewarding good performance and tackling poor performance? Are everyone's performance objectives aligned with the strategic objectives of the organisation?
- Do you reflect the diversity of the customers you serve?

Strategy

Key questions that test current capability

S1 Focus on outcomes

- Do you have a clear, coherent and achievable strategy with a single, overarching set of challenging outcomes, aims, objectives and success measures?
- Is your strategy clear what success looks like and focused on improving the overall quality of life for customers and benefiting the nation?
- How do you negotiate trade-offs between 'priority' outcomes?
- How do you work with your political leadership to develop your strategy?

S2 Base choices on evidence

- How do you understand and respond to what your customers want?
- How do you identify future trends, plan for them and choose between the range of options available?
- How do you ensure that your decisions are informed by sound evidence and analysis?
- How do you cultivate innovative solutions to existing and new problems?

S3 Build common purpose

- How do you engage, align and enthuse partners in the delivery chain to work together as a team to deliver the strategy?
- How do you remove obstacles to effective joint working?
- How do you work with partners when developing strategy?

Delivery

Key questions that test current capability

D1 Plan, resource and prioritise

- Do your business planning processes effectively prioritise and sequence deliverables to deliver your strategic outcomes?
- Are your delivery plans robust, consistent and aligned with the strategy? Taken together, will they effectively deliver all of your strategic outcomes?
- How do you maintain effective control of the organisation's resources? Do your delivery plans include key drivers of cost, with financial implications clearly considered and suitable levels of financial flexibility within the organisation?
- Are your delivery plans regularly reviewed?

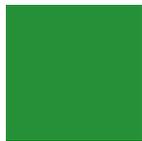
D2 Develop clear roles, responsibilities and delivery model(s)

- Is the purpose of the centre/headquarters functions clear?
- How do you identify and agree roles, responsibilities and accountabilities for delivering your strategic outcomes across the delivery chain? Are these understood and supported by appropriate rewards and incentives, and governance arrangements?
- Do you have clear and well understood delivery models which will deliver your strategic outcomes?
- How do you work with partners to build capability in the delivery chain?

D3 Manage performance

- Do you take personal responsibility for driving performance and striving for excellence across the organisation in pursuit of your strategic outcomes?
- Do you have high-quality, timely and well-understood performance information, supported by analytical capability, which allows you to track performance across the delivery chain? Is performance information aligned with the strategic objectives of the organisation?
- How effectively are programmes and risk managed across the delivery chain? How do you realise and recycle benefits from programmes?
- How do you use financial information to drive greater efficiency and value for money?

Annex B: Assessment categories



Strong – good capability for future delivery in place, in line with the capability model. Clear focus on the action and improvement required to deliver transformation over the medium term.



Well placed – well placed to address any gaps in capability for future delivery through practical actions that are planned or already underway. Is making improvements in capability and is expected to improve further in the medium term.



Development area – the department should be capable of addressing some significant weaknesses in capability for future delivery by taking remedial action. More action is required to close those gaps and deliver improvement over the medium term.



Urgent development area – significant weaknesses in capability for future delivery that require urgent action. Not well placed to address weaknesses and needs significant additional action and support to secure effective delivery. Not well placed to deliver improvement over the medium term.



Serious concerns – serious concerns about current capability. Intervention is required to address current weaknesses and secure improvement in the medium term. (NB only used infrequently, for the most serious gaps.)

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