

External Review

Second 'Updated' Overview Report

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This report contains four sections:

- *Summary of conclusions*
- *Introduction - the economic and policy framework for external review*
- *Review of the theoretical and empirical literature*
- *Comparative examples*

Summary of Conclusions

- The methodology of cost-benefit analysis, properly defined, is well established;
- The application of cost-benefit analysis is under-developed in the appraisal of external review;
- The quantification of costs and benefits to demonstrate the cost-effectiveness of external review is best carried out by the review bodies themselves on an annual basis;
- The framework of incentives and disciplines for the proper preparation and presentation of the costs and benefits of external review can be provided by the Regulatory Impact Assessment (RIA) process;
- Implementation of a balanced system of RIA requirements - with appropriate institutional checks and balances - should help external review evolve to maintain (or achieve) a cost-effective role which provides a good foundation for public confidence;
- Accountability and comparative analysis of RIAs across sectors and review bodies is an essential discipline for developing methodologically sound RIAs and for maximising their contribution to the evolution of cost-effective external review.

Introduction - the economic and policy framework for external review

External review is carried out for a purpose, and should be cost-effective. The Treasury brief therefore aims to address the costs and benefits of external review, and the quantification of those costs and benefits. We start, however, from the position that quantification of costs and benefits has to be set in the wider context of government policy, institutional frameworks and regulatory processes, since these all impinge on the achievement of long run cost-effectiveness.

Preamble

The review of the theoretical and empirical literature demonstrates that the principles of good regulation, and the methodologies available to support rational decision-making, have been well, and fully, explored. The gap is in application. Little more needs to be written about the principles, other than in the context of advice and guidance to bodies applying the principles. It is those bodies which are likely to be in the best position to articulate, quantify, and bring together, the costs and benefits specific to their role in setting up, or running, external review bodies or processes.

The review also shows that particular words are sometimes used in a broad, and sometimes in a restricted, context. This can cause confusion. In particular, we refer here to *cost-benefit analysis* as an all-embracing term for ‘rational’ decision-making. Government self-evidently does not want to proceed with policies where the costs exceed the benefits, everything taken into account. The idea that cost-benefit analysis is a technique applied only to circumstances in which direct financial values can be attributed to the costs and benefits is unhelpful [cost-benefit evaluation of road schemes is a good example where imputed values, such as for time savings, the distinction between the real opportunity cost of resources and transfer payments (such as petrol tax), environmental impact assessments and the forecasting of the ‘counterfactual’, such as the level of congestion without the proposed scheme, are all incorporated into the decision on whether, and with what scheme, to proceed]. Judgements and trade-offs in decisions about whether to have, and what level or type of external review to carry out, will themselves reveal imputed values. The key principle is the honest attempt to include all the costs and benefits which appear relevant to achieving cost-effective external review.

A second example is ‘*audit*’. Traditionally identified with assurance about financial regularity, the word has developed to encompass many forms of review, inspection and certification, whether formal or informal, or involving internal or external reporting. An example is environmental audit (see, for example, the recent report by the Royal Dutch/Shell Group on corporate environmental responsibility).¹ Audit is therefore taken to be a generic term, *equivalent to monitoring*, and which includes both inspection and certification.

¹ People, planet and profits - The Shell Report (full version), www.shell.com (hard copy available).

The hierarchy of regulation

External review is part of the regulatory framework. External Review is not carried out for its own sake, but for a purpose, and therefore has to be set within the broader regulatory context. Its effectiveness therefore has to be judged in its own terms (how effectively does it carry out its specific tasks) and in terms of its contribution to the whole regulatory framework. Three key elements are therefore:

Policy

- responsibility for:
 - the objectives of regulation
 - the rationale for the institutional framework and regulatory scheme adopted
 - the standards or outcomes to be achieved

Control

- monitoring
 - ie, audit, in the sense of *information gathering*, including inspection and certification
- enforcement
 - whether direct requirements or indirect *incentives* (eg, achieving outcomes through a process such as publication of league tables).

Two aspects of these are noteworthy. First, policy can be distinguished from the implementation of controls. Policy is about deciding the regulatory objectives or desirable outcomes; implementation is about the way in which *incentives* on service providers and the controls of the system as a whole (so that control includes external review) operate to achieve the objectives - the desired outcomes - and cost-effectively over time. Secondly, different institutions of government can, and growingly do, take responsibility for different aspects of the policy and control process. Bodies which have responsibility for control processes (either, or both, of monitoring and enforcement) can also have an important advisory role on policy.

Public services are increasingly privately provided, but within a regulatory framework which identifies the conduct (or market) failures to be addressed, builds regulatory policy on that foundation, and separates government responsibility for overall policy from the specific implementation of the regulatory scheme. A good example is provided by utilities and network industry regulation, whereby the main conduct failures can be divided into:

- abuse of monopoly power and anti-competitive practice;
- externalities and public goods (in particular pollution and health and safety aspects);
- social exclusion and inequitable outcomes.

Different institutions take responsibility for each; the 'independent' economic regulators in relation to the first, and government ministers, with their different departments (eg, social security) and agencies (such as the Environment Agency), for the quality and other standards related to the last two. This principle equally applies to other external review bodies and inspectorates, eg, the separation of OFSTED from the DfEE.

Regulation versus inspection

We have made the distinction between policy and control, noting that control incorporates monitoring and enforcement. Monitoring, to have a purpose, must be associated with mechanisms for control and enforcement, whether direct or indirect (hence we described the distinction between the two more as issues of *information gathering* and *incentives*). We noted too that institutional responsibility can be either divided between the two, or one body might be responsible for both. In short, therefore, we would define **Regulators** as *external review bodies with powers of enforcement*. External review alone, including inspection, is a monitoring activity, the information being of use to other bodies who have policy and enforcement responsibilities.

The role of external review bodies and inspectorates has extended in recent years, however, with the development of ‘continuous improvement’ and their use of incentives, particularly publicity and league tables. These incentives become a mechanism for ‘indirect’ enforcement, and therefore the line between external review bodies and regulators becomes increasingly blurred (one test is to ask whether it seems increasingly appropriate to call either, or all of, the NAO, the Audit Commission or OFSTED, regulators?).

The distinction between inspectors and regulators is therefore an important one, and this is built into the framework. Changing roles of traditional external review bodies, however, means that there has to be improved specification of their objectives and roles (which will be assisted by the RIA process), if accountability and cost-effectiveness are to be brought together.

The principles of good regulation

Governments have recognised for a long time the need to manage the regulatory process cost-effectively, and that this involves subjecting itself - as well as others - to various disciplines and incentives. This has found a strong focus in recent years in the work of the Better Regulation Task Force and the Regulatory Impact Unit of the Cabinet Office. The Better Regulation Task Force published its Principles of Good Regulation in 1998, as follows:

- **transparency** - including a clear statement of the objectives of regulation;
- **accountability** - an important discipline!
- **targeting** - one element of cost-effectiveness;
- **consistency** - which should also cover consistency with the objectives of regulation, so that regulation can evolve rather than be ‘consistently’ wrong;
- **proportionality** - another element of cost-effectiveness.

These principles have been the building blocks for procedural developments which link well with other developments in the Modernising Government programme. In particular, the idea of the *Regulatory Impact Assessment (RIA)*, which now has an important formal role in that a minister introducing new regulatory requirements on business has to sign a certificate that to the best of their belief the benefits exceed the costs. To do so, the certificate is supported by paperwork which demonstrates the case, ie, the RIA.² The RIA is particularly relevant to the question of the costs and benefits of external review.

² Cabinet Office (2000), *Good Policy Making: A Guide to Regulatory Impact Assessment*, Modernising Government, the Cabinet office Regulatory Impact Unit.

Process controls in external review - the RIA

The Turnbull Report (September 1999), which followed on from the publication of the Combined Code on Corporate Governance (1998) as a listing requirement for the London Stock Exchange, provides guidance for directors on internal control.³ It puts the management of risk, and the controls to achieve it, at the centre of the Board's responsibilities. The Board is required to be accountable for its management of the internal control process through inspection by external auditors and by publication in the annual report. Turnbull has been judged to be relevant to public bodies (where management of risk could include such things as the Office of the Rail Regulator considering the role of reporting engineers for Railtrack's maintenance programme, or MAFF considering in advance possible controls on the movement of livestock through markets to limit the spread of foot and mouth, should an outbreak occur). Accountability for the management of risk is an important discipline on senior management. The Regulatory Impact Assessment process would have an equivalent effect in the management of regulation and external review of public services, whether privately or publicly provided.

The process controls of a RIA would have utility in providing a more explicit link between the role of government and its departments in setting policy and the role of external review as an element within the overall regulatory jigsaw. It would also provide the foundations for developing experience in the quantification of costs and benefits relevant to the regulated (or reviewed) sector in general. For ministers and governments departments, the RIA would provide the rationalisation for the regulatory and institutional framework established (and as reflected in the relevant statutory powers and duties). For the external reviewing body that RIA would provide the core under-pinning of its 'mission statement', and it would then be required to develop its own annual RIA which would be used to control the review process and to inform the way in which it developed in the future. It could also feed back into reform of the regulatory framework as a whole, for which ministers and other departments would take responsibility.

External reviewing bodies would therefore focus some of their resources on reviewing themselves and incorporating that in an annual RIA, which, in effect, is a cost-benefit report. The external reviewing body is likely to be the best placed to articulate the cost and benefits of its activities, and the discipline of review of its RIA by the body(s) to which it is accountable should ensure - with appropriate safeguards - that the RIA reflects best practice in cost-benefit analysis. The learning process would allow regulation to evolve along the most cost-effective path, and data available to (or collected by) the external reviewing body would maximise the potential degree of quantification of the costs and benefits. A good RIA must include clear evidence of the views and impacts on the body under review (quantified appropriately by performance statistics and opinion surveys, measures of morale, and compliance costs). Commonly reported statements, such as 'we are cost-effective because we only represent a small proportion of the total service spend' would not represent an adequate RIA.

The best outcome will be where the review body positively engages with, and is committed to, the process, such that learning is converted into action aimed at improved cost-

³ ICAEW (1999), Internal control - guidance for Directors on the Combined Code, www.icaew.co.uk/internalcontrol.

effectiveness. The development of 'lighter touch' inspection in education is a good example of how review requirements have (and must have) the capacity to evolve in the light of experience (the cost-benefit test).

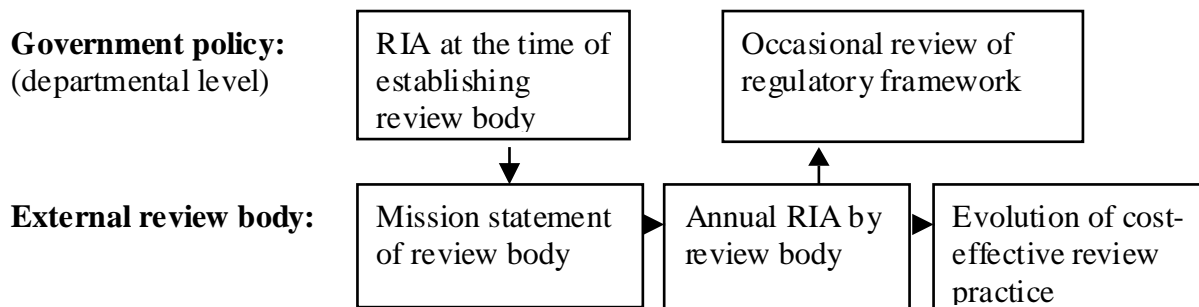
The 'lighter touch' and corporate governance by the service provider

The development of recommendations for corporate governance (Cadbury, Hampel, Turnbull et al) contribute to 'lighter touch' external review and regulation because of their impact on service providers. Review bodies should work within a framework which expects service providers to implement good corporate governance procedures. Since these include verifiable (ie, inspectable) internal controls for the management of risk and the establishment of performance targets, then the review bodies should expect the service providers themselves to have mechanisms to avoid poor outcomes and provide a framework of incentives and targets for achieving outcomes and being accountable for them. If so, 'lighter touch' review and regulation is an inevitable outcome, and the cost-effective role of on-going review becomes inspection of the systems of internal controls and procedures [a well established practice of external financial audit] to ensure that they are sound and operating effectively. Action and further 'heavier-handed' review only occurs when they are found wanting. Service providers should welcome the discipline, and accountability for performance, or non-performance, is more clearly focused on the service provider. A 'lighter touch' evolves therefore *both* because the responsibility for the management and achievement of outcomes is firmly based on the service provider (reinforced by the discipline of external review of the internal controls and corporate governance procedures) and because the review body focuses its other detailed inquiries on those areas which are judged as higher risk or need through a risk assessment or comparative performance review.

Engagement of government and the inspected in the RIA process for external review

The formality of the RIA process has distinct advantages in that it helps 'engage' both the inspected and those ministers and their departments using, and relying on, external review. Where the analysis of costs and benefits fairly covers the impacts on - and of - those inspected, then they are engaged in the process, common views on desired outcomes are debated, consensus begins to emerge, and the friction of review and inspection is reduced because both parties accept the common benefit and the justification of some diversion of resources to implement an RIA process which develops cost-effectiveness in the longer term. Ministers should equally welcome the discipline of an RIA process which helps them demonstrate the rationality and benefits of their policy-making, and helps them avoid discretionary interventions which would likely prove counter-productive. Process and accountability come together to create a 'constructive tension' and dialogue which facilitates the longer run development of clarity of policy objectives about desired outcomes, consensus and cost-effective external review.

The RIA process could be illustrated as:



Is the RIA framework directly transferable?

The Regulatory Impact Assessment guidance developed by the Cabinet Office has become a central focus of the CRI Overview paper because it represents an appropriate ‘framework’ for applying cost-benefit principles to external review in the public sector generally. The current guidance relates to the regulation or deregulation of business, and if the framework of the RIA process were to be applied more widely, then specific guidance for public sector bodies might need to be developed. The overall principles of the RIA framework, however, are unaffected, which we sum up as *cost-benefit analysis with process*. The discipline and accountability of the process - to examine in a comprehensive way the costs and benefits of external review - should enable a ‘learning process’ over time which helps develop cost-effective external review. A different name could be sought when applied to public bodies more generally (eg, Review Impact Assessment) but this would seem to be unnecessary as RIA is a good, generic term, even though it was developed in a specific setting.

External review and policy advice

External review bodies may be responsible for a number of activities, not the least of which may be - through the monitoring process of inspection and review - advising government on the way in which current policies are working in practice and how ministers might consider changing them, or the instruments applied. The RIA process - which is directed at evaluating the current set of government policies and standards - for which external review is one part of the jigsaw - will assist that ‘advisory role’, but is not a cost-based analysis of the advisory role itself. The context for the RIA process in policy advice is therefore the Principles of Better Regulation as articulated by the Better Regulation Task Force, with a particular focus in this context on ‘targeting’ and ‘proportionality’ of the regulatory instruments and policies in force.

Publication, accountability and confidence

The RIA by the external reviewing body will identify the costs and benefits of its activities, with a particular focus on the cost-effectiveness of the burdens imposed by review and the degree of alignment of the incentives imposed by external review with the ‘desired’ outcomes. Perverse regulatory incentives should be eliminated over time. In a similar way the external reviewing body must itself have the right incentives to produce a balanced, complete, and quantified (including description where necessary) cost-benefit assessment for its RIA. It will, of course, be commented, that the body will only have an interest to justify its past regulatory actions, something which may be rationalised in terms of maintaining public confidence.

Submission to the sponsoring department, to which it is accountable, will be the first discipline (noting that each department now has its own Regulatory Impact Unit arising out of the Cabinet Office advice and requirements on RIAs for business regulation as part of the modernising government programme). Another is that, in any event, it is the long term interest of both bodies to promote cost-effective review and control. However, it will also be commented that the sponsoring department set up the review body, and hence will be protective of it, lest it brings blame on itself, or equally is concerned with undermining public confidence. The latter is a self-defeating argument, which simply stores up problems for the future, but it would be important to recognise that some further discipline on ensuring good practice is imposed. This could involve one or more of:

- Departmental select committees having access to the RIAs, and using them in their scrutiny of departmental performance;
- A non-sponsoring department of government taking responsibility for comparative analysis of RIAs, such as the Treasury or the Cabinet Office;
- Explicit linkage between the RIA and the review body's forward work programmes, with the associated discipline and opportunities related to budget approval by the Treasury;
- National Audit Office (an office of Parliament) developing a particular expertise in the analysis of the cost-benefit of external review by RIAs through its value for money (VFM) studies (NAO would itself be subject to the RIA process);
- Publication of the RIA in the review body's annual report.

The checks and balances which ensure the evolution of best and cost-effective practice in external review, whilst maintaining public confidence and the authority of the review process, is an important issue for government to consider.

Checks and balances - comparative analysis

Checks and balances will be required if external review bodies (inspectorates) and regulators are to be expected to play a key role in the development of RIAs for their activities. Reference was made above to non-sponsoring government departments having responsibility for comparative analysis. It would be useful to consider different specialisms, eg:

Cabinet Office - the methodology of the RIA (which we might sum up as '*cost-benefit analysis with process*', the formality of the process being an important discipline on the preparer to produce a balanced and comprehensive RIA).

HM Treasury - the link between RIAs, forward programmes and budget approval (with sponsoring departments as part of the public expenditure control (PESC) process).

NAO - the comparative analysis of RIAs once produced, as a cross-cutting review exercise to inform generally both departmental select committee work and the NAO's own targeted VFM studies for the PAC.

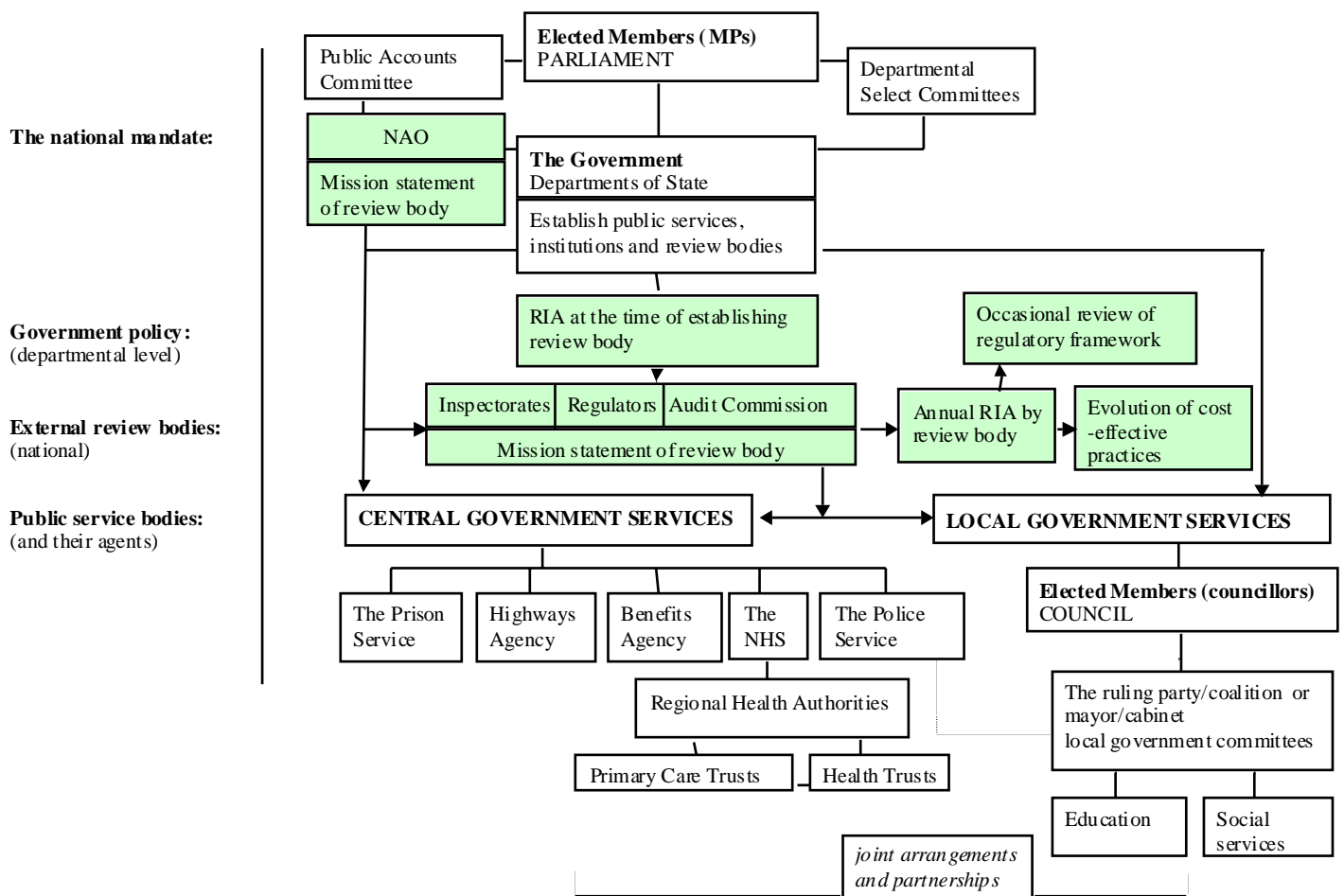
Multiple accountabilities - national and local government

A key aspect of the framework is identification of the 'policy maker' and the role of setting standards (minimum requirements) and targets (future, improved standards). Review bodies (inspectorates) and regulators are 'national' bodies, and fit well within the national

institutional framework as a whole. So far this context has been taken as read, only focusing on the RIA process as a flow diagram of five boxes under process controls, which placed government policy and external review/regulation at different levels.

The following diagram, **Setting the RIA process in context**, sets those boxes (shaded in to identify them above) in the wider institutional context of central and local government. The only caveat which we would add is that where local government has ‘policy discretion’ over certain standards, and national government does not intend to question decisions made under that policy discretion, then any national review body must be able to properly distinguish between national and local standards. The continuous improvement role should only apply to nationally determined and accountable targets. If conflicting standards and responsibilities appear between national and local government, then the RIA process should help identify and eliminate them, by a clear separation of roles and responsibilities. Other examples, such as the NHS and the police service, seem to fit equally well into the general framework set out in the following diagram.

Setting the RIA process in context



Standards and roles

Transparency and accountability requires that the roles of each party in the regulatory jigsaw are well understood. The review of the theoretical and empirical literature and the comparative examples show clearly that a clear distinction must be made between the role of external review in avoiding detrimental or unsatisfactory outcomes, which thereby give confidence and assurance, and the role of promoting higher standards. The former is well-founded and understandable (although it could be argued it involves only a focus on 'bad outcomes' which might affect confidence generally). The latter, however, may benefit most from the introduction of the rigour of RIAs. The concept of 'continuous improvement', whilst it may be seen to have a link with competitive market systems, and uses the review body as a 'surrogate' for competition, can obscure the link between the cost-benefit test on the particular standard to be achieved, and transfer accountability from the department and the minister to the external review body. If there is to be 'improvement', then the prospective standard, and its associated cost-benefit test, have to be clearly articulated by the standard setter (such that continuous improvement has a limit after the target has been achieved), given that review bodies may not have the automatic discipline on them to have regard to the costs which 'new entrants' to a competitive market clearly have. This may lead to ever more burdensome and demoralising exhortation by review bodies, uncaring and unaccountable for the costs and benefits of their activities.

Continuous improvement versus assurance

The issue of changing institutional roles has been noted, and one problem identified; the concern being that the term continuous improvement can obscure the need for a clear target on the future, improved standards to be achieved, otherwise the process is too 'open-ended' and unaccountable. A distinction should also be made between continuous improvement of standards themselves, and improvements in the cost-effective delivery of a set standard. The role of fostering continuous improvement, as noted above, can be incorporated within the general framework, but there needs to be clarity of objectives where review bodies play multiple roles, and in particular where those roles have developed to include surrogate, indirect enforcement mechanisms through incentives, such as 'name and shame'. This development does not, therefore, change the framework, but exposes the need for process mechanisms, such as the RIA, which focus on accountability and can act as a catalyst (or trigger) for policy review of what might have become an uncontrolled, unaccountable, and burdensome, role.

Review of the theoretical and empirical literature

Context

Between the mid-1970s and 1997, there was a rise in so-called New Public Management (that is, decentralisation of decision-making to public service managers (a philosophy of “let managers manage”)), coupled with a proliferation of public sector regulators, in particular external inspection bodies.⁴ This public sector regulation⁵ was characterised by a number of factors, including:

- ad hoc and unrationalised growth in regulation, while public service staff declined;
- an increase in formality, complexity, intensity and specialisation of public sector regulation, in particular in those sectors removed from central government.⁶

As a result, public sector regulation amounts to a large enterprise, with government investing more resources (in staff and public spending) in regulating itself than it does in regulating the privatised utilities.⁷ But while the burdens of private sector regulation have been well-discussed and researched, there is far less research on the burdens of public sector regulation.

This trend in growth of public sector regulation has continued since 1997, with the addition of new regulators and the extension of external inspection across the public sector, with many services being inspected for the first time (for example, through the Better Value Inspectorate and the Commission for Health Improvement).⁸ The system of public sector regulation developed between the mid-1970s and 1997 is argued to have involved, in general, more formalistic and heavy-duty regulation over local government and the outer reaches of the public sector than of core central government departments. Since 1997, the government has broadly maintained this pattern and local public bodies and the mixed public/private sector are argued to have borne the brunt of planned regulatory increases rather than core central government departments. For example, the Modernising Government process suggests that while core departments be subject to regulation through ‘peer review’, other parts of the public sector be subject to a much harder line approach (for example, the extension of the heavy-duty OFSTED school inspection regime and the adoption of Best Value policy for local authorities has substantially broadened the scope of audit of local authorities by central bodies).

It has been argued, however, that while the style of regulatory growth prior to 1997 was unacknowledged and unrationalised, since 1997 government has adopted a philosophy which acknowledges the compliance cost problem associated with public-sector regulation, expresses concern with the consistency of practice and linkages amongst different regulators (and proposed more co-ordination of inspection functions with the development of a common set of inspection principles, and established the Public Audit Forum and the Best Value Inspectorate Forum to help achieve this), and embraces a doctrine of “enforced self-

⁴ Hood, C, James, O and Scott, C (2000)

⁵ In this context, the term regulation is defined loosely to include the activities of monitoring and review.

⁶ Hood, C, James, O, Jones, G, Scott, C and Travers, T (1998)

⁷ Ibid.

⁸ Martin, S Inspecting the inspectors. *Public Finance*.

regulation”.⁹ Enforced self-regulation can be defined as “intervening in inverse proportion to success and striking an appropriate balance between intervening where services are failing and giving successful organisations the freedom to manage”.¹⁰ In other words, the enforced self-regulation doctrine involves the deployment of heavier regulatory tackle against the incompetent or recalcitrant, while lightening the regulatory yoke over good performers.

The impact of public sector audit on those bodies being reviewed has been gaining increasing attention in recent months. This has included a proliferation of reports emerging from both central government and local government. The foci of the documentation range from an evaluation of the role of leadership and risk management (internal control) in improving public service performance to the scrutiny of local government authorities responses to audit and inspection regimes (external control). Implicitly, these reports tend to show a growing support for greater decentralisation of power and less rigid audit and inspection regimes. They question the link between audit or inspection and improvement of public services and call for a more balanced approach to the application of centralised regulation within the public sector. This is supported by an increasingly high profile lobby against the burdens of inspection and audit, in particular in the education sector, which has been picked up by the media. For example, the recent highly publicised debate on inspection in higher education universities and colleges.

What are the different elements of external review?

External review can be defined as ‘oversight of bureaucracies by other public agencies operating at arm’s length from the direct line of command, the overseers being endowed with some sort of official authority over their charges’, with the three essential defining elements, all of which must be present, being:

- one public bureaucracy in the role of an overseer aiming to shape the activities of another;
- an organisational separation between the ‘regulating’ bureaucracy and the ‘regulatee’ with the regulator outside the direct line of command (this feature distinguishes intra-organisational controls from arm’s length oversight by another organisation);
- some official mandate for the regulator organisation to scrutinise the behaviour of the regulatee and seek to change it.¹¹

Hood and Scott (2000) identify a range of bodies operating in the sphere of public sector regulation. Apart from parliamentary and judicial review bodies, they include bureaucratic agents of legislators, such as parliamentary auditors, review bodies quasi-independent from the regular government structure, such as prison or education inspectors, standard units with regulatory roles, such as central government departments overseeing other levels and units in government, and bodies that regulate both private and public sector organisations, for example data protection, equal opportunities, health and safety at work and industry-specific regulators where there are both public and private sector providers, for example prisons and social services. The Table below details a full range of regulatory bodies.¹²

⁹ Ibid.

¹⁰ Modernising Government White Paper.

¹¹ Hood et al (1998).

¹² Hood et al (1998).

Type of regulatory bodies	Examples
Parliamentary review bodies	Elected representatives in legislatures and, in particular, Select Committees, such as the Public Accounts Committee
Judicial review bodies	Law courts and independent judiciary
Public audit bodies	National Audit Office, Audit Commission, Accounts Commission for Scotland, the Northern Ireland Audit Office
Inspectorates and equivalents	OFSTED, Better Value Inspectorate, Social Services Inspectorate, Prisons Inspectorate, HM Inspectorate of Constabulary, Benefit Fraud Inspectorate, HM Fire Services Inspectorate
Ombudsmen and grievance handlers	
Central agency regulators	Units in the Treasury
Funders-cum-regulators	Higher Education Funding Councils and the Housing Corporation
Other central government regulators	Units over-seeing executive agencies
Central regulators of local public bodies and the NHS	Commission for Health Improvement
Other (within broader definition of regulation)	Specialised administrative tribunals, regulators of public utilities, supra-national regulators at the EU level, regulators which operated both in the public and private sphere and regulators inside local government

This study, however, focuses on those bodies responsible for external review of public sector performance, specifically those with a standing remit to review performance. There are, however, certain definitional questions that remain:

- how is *external* defined, that is how are the boundaries of an organisation defined;
- does *public sector* include regulators of private sector providers of public services (for example, utility sector regulators) or regulators of mixed public and private-sector providers (for example, the Social Services Inspectorate which extends to providers outside the public sector, or the Health and Safety Executive, which regulates health and safety at work in both public and private sector organisations);
- does the term *standing remit* extend to non-government bodies who review public services (for example, the Association of Chief Police Officers).

For the purposes of this project, the Public Services Productivity Panel Unit have defined public sector to exclude the regulation of private sector providers of public services (for example, economic regulators). In addition, the project also explicitly calls for a focus on inspection and external review, rather than the broader term regulation.

This raises a definitional question with regard to the terms regulation, audit and inspection. In their work, the Audit Commission makes a distinction between *audit* and *inspection*. Others define *certification* as a separate regulatory activity from audit and inspection.¹³ The lines

¹³ Other regulatory activities include *adjudication* or mediation and *authorisation*.

between these different categories of external review are, however, agreed to be blurred and overlapping.

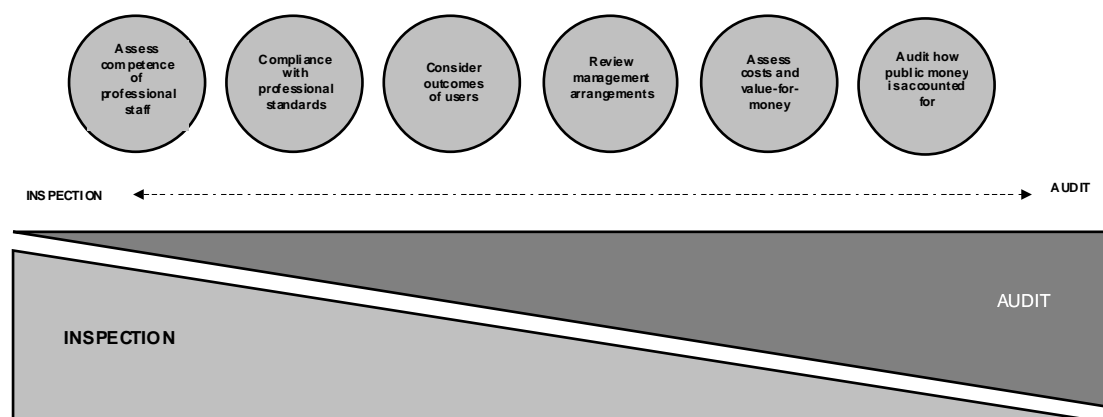
The Audit Commission defines the principle differences between inspection and audit as being:

- the emphasis of *audit* is on money
- the emphasis of *inspection* is on standards.¹⁴

Acknowledging that the roles of audit and inspection bodies increasingly overlap, the Audit Commission defines auditing and inspection in the following manner:

- *Auditing* reports on how public money has been accounted for and on the overall financial health of a public body, and has a particular role in considering costs and value for money and commenting on the three E's (economy, efficiency and effectiveness). However, some inspectorates also account for public money (such as the Benefits Fraud Inspectorate which considers how benefit payments are accounted for) and inspectorates are increasingly considering VFM as well.
- *Inspection* assesses how individuals deliver best professional practice (this is not a role of auditors, although they do comment on the financial competence of a wide range of managers) and comments on how well an organisation complies with best professional practice (when considering efficiency and effectiveness, however, auditors may also consider how best practice is applied).

The Audit Commission state that auditors and inspectors differ in the way in which they work – auditors provide a continuous presence, only occasionally investigating in great depth where they are major concerns relating to public money or propriety, while inspection is periodic, operating over a longer cycle and investigating routinely in greater depth and with a particular professional focus. Central to both audit and inspection is the consideration of outcomes. For example, inspections consider quality of outcomes and outputs and auditors also consider outcomes in their VFM work. Both auditors and inspectors also review how well management is organised. While inspectors focus on management of a specific service or profession, auditors focus on overall financial and management arrangements of a public body. The Audit Commission view inspection and audit as a continuum as demonstrated below.¹⁵



¹⁴ Audit Commission *The Audit Commission: Developing principles for public inspection. A consultation document.*

¹⁵ Ibid.

Certification is the official declaration of the fitness or quality of some individual, organisation or object. Certification overlaps with audit as auditors issue certificates. Certification procedures have been applied to the regulation of the public service, for example, the issuing of police efficiency certificates. Vinten (1998) defines certification as a dependent, systems-oriented, generalist practice which produces comfort certificates at an acceptable cost.

It can be argued, however, that while audit and inspection can be distinguished from one another where audit is concerned entirely with financial propriety or regularity, as audit has become increasingly concerned with value-for-money and inspection with performance auditing, the differences between the two are less distinguishable. Furthermore, inspection and certification may also be seen as natural parts of the auditing process.

Style of regulation by external reviewers

Regulators vary widely in the formality and punitiveness with which they approach those they regulate. There is no style guide for public sector regulators; and there is no consistency between the operations and sanctions of the different public-sector regulators.¹⁶ This lack of consistency may make it more difficult to determine the effectiveness of external review and the particular costs and benefits associated with different styles. Fora, such as the Public Audit Forum and the Best Value Inspectorate Forum, which provide space for auditors and inspectors to co-operate and to develop best practice to enhance the efficiency and effectiveness of their own organisations may increase consistency. It has been argued, however, that the Public Audit Forum does not appear to challenge the differences between the audit bodies, but rather provides a reassuring framework which reconciles these differences; and does not address the questions of burden of audit and inspection.¹⁷ These fora have also been criticised on the basis that they do not span across the various domains of regulation, that is they allow for interaction between either auditors or inspectors, but there is no scope for discussion across the different types of review bodies.¹⁸ Public sector reviewees complain of being over-audited, of a lack of co-ordination between the work of different auditors, and of multiple sources of demands for information. A consistent and co-ordinated approach across and between the different external review bodies is required to address this regulatory burden.

It is also argued that there is a difference in style of regulation applied to central government and that applied to local government and the mixed public-private sector – with more formal and heavy-duty regulation over local government and the outer reaches of the public sector than of core central government departments.¹⁹ A thesis of social relational distance is applied to understanding this disparity.²⁰ Where the social distance between the regulator and the regulatee is greatest, it is argued, regulatory behaviour tends to be most formal.²¹ This is

¹⁶ Travers, T Where now for the watchdogs? *PubNet*.

¹⁷ Bowerman, M Behind the public image: An analysis of enduring concerns about public audit, *Public Management and Policy Association*.

¹⁸ Hood et al (2000).

¹⁹ Hood et al (1998).

²⁰ That is, the more distant regulators are from their clients backgrounds, the more formally they behave (in the sense of non-participatory standard-setting, rule-bound regulatory behaviour and heavy reliance on formal reporting and sanctioning, rather than participating, discretionary regulation with co-operative methods for gathering information and modifying behaviour).

²¹ Hood et al (1998).

believed to increase the compliance costs of the regulation, but there have been no empirical studies to support this evidence.

The style of individual regulators also varies. For example, the naming and shaming of schools by OFSTED versus softer approaches of other inspectorates. There is no analysis to determine which of these styles is the most appropriate.

Why regulate: The role of external review

The public sector analogy to market failure is the idea of government failure. Public sector externalities arise where control and performance appraisal systems fail to reflect the wider effect of a public organisation's activities on the goals of other organisations. Other failures arise where bureaucrats can exploit their monopoly position as providers of a service or where bureaucratic agents can exploit principals because they have an informational advantage about the activity they are performing. The consequences of these failures include goal displacement where the aims of a public body are altered by those running it, under- or over-supply of public services where too much or too little is produced, wasteful production where services are produced at a cost in excess of what could be achieved and difficulties in ensuring the quality of public services.²² The role of public sector regulation is to help mitigate these failures. It can improve the treatment of externalities by regulators by introducing rules to encourage organisations to take account of their activities on other bodies and through regulators spreading information about the effects of different bodies' actions on other parts of the public sector. Monitoring by regulators helps to penetrate information asymmetry, and expose fraudulent and wasteful behaviour by external verification of costs and performance. Regulators can also uncover cost-padding and evaluate the quality of services.

Roles of external inspection of public services are to provide assurance about the standard of performance achieved and the prospects of improvement and to provide independent assessment of performance and organisational health that can be instrumental in shaping plans for improvement.²³ External review also aims to increase public accountability by holding public sector bodies to account for their decisions and actions, including setting and achieving operational objectives and priorities, proper and efficient use of public money, management processes, and quality of services provided. External review also evaluates regularity or legality, probity (that is, honesty and integrity or the avoidance of fraud and corruption), and value for money (that is, securing economy, efficiency and effectiveness in the use of resources).

The way in which public sector performance is evaluated varies. For example, until recently, most of the local government inspection regimes (Ofsted, Social Services Inspectorate, HM Fire Inspectorate) were designed to ensure that services were not falling below specified minimum standards (that is, their aim is to root out failure). New inspectorates (for example, Best Value Inspectorate and Commission for Health Improvement) are charged with ensuring that there is continuous improvement in service quality and cost-effectiveness (that is, their aim is to facilitate improvement by encouraging local capacity to change). Inspection criteria are also changing – traditionally focused on past performance and used measures of resource inputs and internal processes, whereas now aiming to focus on judging the capacity to

²² James (2000).

²³ Institute for Public Policy Research et al (2000).

achieve future targets for improvement and focusing on outcomes.²⁴ This shift in approach could affect the way in which the effectiveness of external review is evaluated, as well as the way in which costs and benefits are measured.

The role of audit in evaluating performance is controversial, in particular when linked to rewards and punishments. It is argued that as some aspects of performance are difficult to capture, there is a tendency to measure those aspects which are easy to measure; as a result these are not definitive rankings of who should receive punishment and reward.²⁵

Costs and benefits

Much of the literature reviewed criticises the fact that the external reviewers or regulators do not apply their own standards of good practice to themselves – that is, they do not demonstrate their own effectiveness or assess the burden of their regulatory activities to the regulated bodies. Hood et al (1998), for example, state “the structure of regulation for efficiency in Government – as pursued by VFM auditing and various quality and efficiency regulators – seems to reflect an implicit belief that duplication, overlap and unrationalised proliferation of separate units making costly demands on their regulatory charges promotes value for money – there is no co-ordination or information sharing between regulatory bodies for public sector review to develop good practice.” The Public Audit Forum and the Better Value Inspectorate have, however, been set up in an attempt to co-ordinate practice between regulatory bodies and provide more joined-up government.

However, there is very little literature on the burden of regulation and the application of existing methodologies to assessing this burden. James (2000) argues that “we are at a very early stage in developing theories to explain why regulation develops and to evaluate the costs and benefits of the activity.” This is true when comparing the state of the literature on the public sector with that to the much more developed literature on the regulation of the private sector. The criticisms of external review of the public sector do, however, point to some of the costs to the system.

Demands for information or scrutinies from Whitehall and other external review agencies are seen by many of the regulated bodies as being repetitive and irrelevant. It is argued that too much calling to account may confuse the issue of who is responsible and may impede the ability of management of an organisation to run the services for which they are held accountable. There are concerns about the repetition of requests for information, the inappropriateness of some department-wide or system-wide requests or scrutinies, the multiple sources of demands for information and overlapping accountability requirements.²⁶ The regulated bodies also complain of the costs and staff time involved in dealing with regulators.²⁷ Parliamentary review of public sector agencies is also criticised for being inconsistent – some bodies, such as the prison service, benefits agency and child support agency, are under deep scrutiny by parliament, while others escape Parliamentary scrutiny.

²⁴ Martin, S Inspecting the inspectors. *Public Finance*.

²⁵ Bowerman, M Behind the public image: An analysis of enduring concerns about public audit, *Public Management and Policy Association*.

²⁶ Hogwood, B et al The audit of accountability, *PubNet*.

²⁷ Hood et al (1998).

Modernising Government proposed the application of oversight and review to regulation of government (that is, the development of common codes of conduct and concern with cost-effectiveness), but no coherent principles were offered as to when enforced self regulation was appropriate or what its scope and limits should be in government. There were no arrangements for overall co-ordination and evaluation of regulatory burdens placed on public organisations. There were no systems for logging compliance costs and conducting regulatory impact analysis. There is a continuing evidence vacuum about the marginal effects (positive or negative) of increasing or reducing investment in regulation of government. Analysis of Regulatory Impact Assessment in business regulation – what is done to ensure that regulatory compliance is taken account of in the regulation of business and what is done to ensure mutuality between different regulators – may be useful to provide pointers as to the costs and benefits of public sector regulation.

The Audit Commission does include a statement of the cost-benefit test in its principles for audit, stating that “inspection and compliance should cost less than the potential gains achievable through improvement.” The cost of inspection can, therefore, only be justified if it can be shown to bring a return through improvement in service effectiveness and efficiency. The IPPR (2000) argue, however, that the link between inspection and improvement depends heavily on the attitudes and approach of the inspected and inspectors. The contribution of inspection, therefore, needs to be assessed in the broader context of how organisations improve, including the role of peer review and other voluntary processes of external comparison and assessment.²⁸

Costs

- Direct costs

Includes the direct costs of staff and the operational costs of the external review body/regulator; or for review bodies that co-opt private sector auditors, for example, and review a range of different government sectors, the costs of undertaking the review of a particular service. These are the simplest costs to determine and can be expected to be largely collected and accounted for.

- Compliance costs

Compliance costs are what it costs the regulated bodies to meet the requirements of those who regulate them. These costs are not routinely collected across government and, therefore, are more difficult to estimate. Compliance costs include what it costs the regulated bodies to interact with the external review body/regulator, including any additional costs involved in the provision of the information requested, consultation with the external reviewer, and acting as guides on visits and inspections.²⁹

Compliance costs are argued to be growing because of more formal regulation which leads to increased procedural constraints. The increased formality of controls and explosion of controls for making things auditable combined with an increase in mistrust of professional self regulation is argued to result in increased regulation and increased compliance costs.

²⁸ Institute for Public Policy Research et al (2000).

²⁹ Hood et al (1998).

Compliance costs are also argued to be higher as a result of a lack of consistency between external review bodies, although there is no empirical evidence to support this.

- Behavioural costs

Behavioural costs are the effects on the organisation being reviewed, such as lack of innovation, colonisation and decoupling.

- *Colonisation*: Occurs when the reviewer's values and interests begin to supplant those of the reviewee. Thus organisations start to focus upon documenting processes and levels of direct output rather than results in outcome terms. This may be particularly the case where review tends to be compliance focused. A further manifestation is the production of data purely for the benefit of reviewers. The concentration on approved process and output data may, in turn, result in the displacement of more effective quality improvement efforts.
- *Decoupling*: Occurs where the impact of the review is deliberately marginalised. Manifestations include the creation of buffer organisations (such as internal review mechanisms) and the reduction of review activities towards the ceremonial or ritual.
- *Inability to take risks*: External review may result in an unwillingness for public servants to take risk for fear of falling under the glare of public scrutiny or being prey to governmental intervention. Vincent (1996) argues that accountability should be the basis from which to learn how best to achieve desired outcomes effectively and efficiently and therefore "a wise course of action is for public leaders and managers is a strategy of small mistakes."³⁰ He argues that the public sector is a particularly hard place for people to take risks – and therefore learn – without punishment. Regulation should recognise that mistakes will be made, but should not be made repeatedly and, therefore, public organisations and their employees should be allowed to make enough small mistakes to learn, but not enough mistakes to be punished. He argues further that a fundamental conflict exists between granting freedom to take risks (through new public management and the devolution of authority to public sector managers) and ensuring accountability and control (through, for example, external review agencies, which set rules and parameters within which risk may be taken). The NAO report on *Supporting innovation: Managing risk in government departments* states that risk management can help departments improve their performance in a number of ways: it can lead to better service delivery, more efficient use of resources, better project management, help minimise waste, fraud and poor value for money, and promote innovation. Citizens and businesses can waste time and lose out financially if public services are inadequate or inefficiently delivered. And the reputation of departments can suffer where services fail to meet the public's expectations. Assessing the risk of such circumstances arising can help departments ensure that they have adequate arrangements in place to deal with them or with something coming out of the blue. They argue that a barrier to risk taking is that the status and activities of public bodies limits the risk departments can take with public services. An incentive to risk taking would be the dissemination of good practice on business risk management with examples of where it has added value, providing guidance and advice on risk management and clarification of individual responsibilities and accountabilities for key risks. They identify the requirements for risk management to be effective and innovation to be encouraged as – risk management policies and the benefits of effective risk management should be clearly communicated to staff, senior

³⁰ Vincent, J (1996).

management needs to support and promote risk management, the department's culture should support well thought through risk taking and innovation, risk management should be embedded in management processes, the management of risk should be closely linked to the achievement of objectives, and risks associated with working with other organisations should be assessed and managed.

- Associated with an inability to take risks is a *lack of innovation*. Use of fear of failure as an external incentive can suppress innovation and social entrepreneurship by discouraging risk taking. A recent PIU report points to the blame culture in public sector, arguing that the public sector tends to be intolerant of failure and can make people working in the sector overly cautious about trying new and different approaches. The attempt to eliminate failure can hamper the development of leadership and prevent the creation of learning organisations. The PIU argue that “leaders are not always given enough space to lead – almost by definition leadership involves making choice, rather than solely an agent for decisions made elsewhere. Excessively tight control, and the coexistence of multiple levers of central control, can easily corrode the capacity to lead.”³¹
- *Undermining of trust*: Decline in organisational trust which creates an inhibiting and anxious pre-occupation with how one is seen by others.³²
- *Impression management*: Concentration on good PR and managing reviewer's visits.
- *Management abrogation*: Where managers fail to address issues and risks on the grounds that the reviewer will tell them if there is a problem.

- Opportunity costs

One cannot look at the cost of the review activity in isolation; need to evaluate the costs of the activity in relation to doing something different, for example of services not delivered to clients because staff were otherwise engaged.

In addition, the cost of the review activity should be assessed against alternative review strategies or alternatives to regulation, for example the cost of external review by several bodies versus the cost of external review by joined-up bodies or the cost of internal management/self-regulation versus the cost of external review.

Benefits

Costing of the benefits of external review is even less well-covered in the theoretical literature than of the costs. In general terms, the benefits are considered to be deterrance (avoidance of adverse outcomes that would otherwise occur) and comfort or assurance about organisational products or processes. These are particularly difficult concepts to quantify and, therefore, it is often argued that it is impossible to assess the effectiveness of external review. Power (1997), for example, argues that assurance is likely to be illusory because it rests on rituals of controlling the control rather than direct observation.

The starting point for identifying benefits is to determine to whom the expected benefits are likely to accrue – government, tax payers, users etc. For example, for government the benefits of external review may include an appearance of increase public accountability (public image) and increased public confidence. For tax payers, the benefits include better use of public resources (an improvement in cost-effectiveness of service provision) and associated

³¹ Performance and Innovation Unit (2001) *Strengthening leadership in the public sector*.

³² Power (1997)

comfort. For users, the benefits may include improved service delivery, an increase in choice or a change in scope and focus of service provision. For the public sector body under scrutiny, the benefits may include improved management and more productive staff.

The costs and benefits of external review should be considered in relation to the overall aims and objectives of the audit or inspection bodies. One of the key aims of audit and inspection is to improve the delivery of services by public bodies. However, the link between inspection or audit and improvement is difficult to prove. A recent study by the Local Government Association³³ on the perceptions of local authorities on inspection found that local authorities saw government inspection as an essential road to improvement, but that it is failing to act as the catalyst for improvement that it might. The survey found that over 70% of respondents felt that inspection was an important catalyst for improvement and increased accountability, but less than half felt that inspection resulted in service improvement and only 27% thought it led to innovation.³⁴

It is important to keep under consideration, when identifying costs and, in particular, benefits the tendency toward focusing on those costs and benefits which are quantifiable or measurable; and to seek to identify the qualitative impacts as well. This is particularly important with regard to the benefits of external review, which often appear harder to define and to measure. For example, how do you measure comfort/assurance? How do you apportion the benefits of service improvements between the internal management process and the external review process?

Measuring the costs and benefits

There are several Government documents which provide guidance on appraisal and evaluation in public sector decision-making. These include:

- HM Treasury (1997) *The Green Book: Appraisal and evaluation in central government*.
- Department of Environment, Transport and the Regions *Multi-criteria analysis: A manual*.
- Regulatory Impact Unit *Good policy making: A guide to Regulatory Impact Assessment*.

These documents cover methodologies for both monetary and non-monetary evaluation of costs and benefits.

Monetary valuations

Cost-Benefit analysis (CBA)

An assessment of the costs and benefits of alternative options. CBA explicitly values non-marketed outputs in money terms. CBA seeks to value the expected impacts of an option in monetary terms. These valuations are based on well-developed economic theory of valuation based on willingness-to-pay or to accept. In principle, a project is desirable if the benefits exceed the losses, suitably discounted over time.

³³ Local Government Association (2001) *An inspector calls: A survey of local authorities on the impact of inspection*.

³⁴ PubNet (2001) *Inspection only partially delivering*, Tuesday, 3 April 2001.

In practice, it is hardly ever realistic to value all the costs and benefits of options in monetary terms. Most CBAs will incorporate some additional items which it is either not possible to value, or not economic to do so. But where the most important costs and benefits have been valued, the others can be set alongside and included in the decision process.

The *HM Treasury Green Book* provides a comprehensive guide to the methodological application of cost-benefit analysis.

Regulatory Impact Assessment (RIA)

RIA is a type of cost-benefit analysis. It is a policy tool which assesses the impact, in terms of costs, benefits and risks of any proposed regulation.

The Cabinet Office's Regulatory Impact Unit has produced a guide to RIA for regulation of businesses, charities and the voluntary sector, entitled *Good policy making: A guide to Regulatory Impact Assessment*. The key elements of the RIA are identified as:

- includes an *assessment of risks* that the proposed regulation is addressing – that is, identification of the hazard or situation which, in particular circumstances, leads to harm or detriment, and estimating the probability that the detriment or harm occurs (where risks are difficult to quantify, qualitative data should be used; a time element should be attached to the risk assessment)
- identification of *benefits* associated with each option – whenever feasible, a fully quantitative analysis of benefits should be carried out; benefits should be represented in a quantified (and preferably monetary) format as by failing to provide any quantifiable measure of benefits, whilst at the same time providing detailed estimates of costs, the proposal will be unbalanced with costs appearing to clearly outweigh benefits (valuing benefits can, however, be often difficult and, at times, highly subjective)
- identification of *costs* associated with each option – broken down into policy and implementation cost and including both direct and indirect costs
- *securing compliance*

The RIA refers to the HM Treasury 'Green Book' for methodologies on quantifying and valuing costs and benefits and provides the following guidance on assessing the costs and benefits:

For *benefits*:

- identify who is likely to benefit from the regulatory proposal and estimate numbers involved
- identify the benefits of each option to each group affected
- assess the actual benefits for each of the options over the expected life of the proposals (including both immediate or "direct benefits" and "indirect benefits")
- express, as far as possible, the benefits in monetary terms
- when valuation is not possible, it may still be possible to quantify benefits – for example, there are a number of qualitative indices of noise nuisance, levels of pollution

For *costs*:

- identify who bears the costs
- identify how these costs vary according to the various options
- quantifying and valuing the costs, taking into account:

- ⇒ distinguish between policy (costs that can be directly attributed to the policy goal) and implementation (costs associated with the implementation of regulation or red-tape burden of regulation) costs
- ⇒ identify the distribution of costs between different bodies
- ⇒ identify and, where possible, quantify any other additional costs (to the environment or consumers, for example) and any indirect costs
- ⇒ identify costs to vulnerable people/groups
- ⇒ identify the costs to government
- ⇒ identify the costs of compliance (for example, paperwork requirements, record keeping, provision of statutory returns, visits etc)
- provide the total cost, that is not just the impact on one company, but on all businesses

Cost-effectiveness analysis (CEA)

Compares the costs of alternative ways of providing similar kinds of output/the same objective. Any differences in output are compared subjectively with the differences in cost.

Where there are alternative options to achieve a specific objective, but where the objective itself cannot be valued, CEA is used to assess the least-cost way of achieving the objective. CEA includes opportunity costs, some external costs (where they are straightforward to value), and may include shadow prices for some marketed outputs.

CEA is the most common form of analysis in government and the Treasury ‘Green Book’ on *Appraisal and evaluation in Central Government* is most frequently applied to CEA. The Treasury’s “Green Book” provides a methodology for appraising costs and benefits of the following activities: policy development, capital projects, existing assets and specification of standards, such as the choice of standards for health and safety, or to balance compliance costs with the benefits of regulation. The ‘Green Book’ states appraisal is not costless – the effort that should go into them and the detail to be considered is a matter of judgement. The ‘Green Book’ also provides guidance on the application of different types of methodologies to different types of information or activities – cost effectiveness analysis versus cost-benefit analysis for example.

Financial analysis

An assessment of the impact of an option on the decision-making organisation’s own financial costs and revenues. Financial analysis of the impacts of a proposal on a department’s own budget and on public expenditure includes Regulatory Impact Assessments.

Non-monetary valuation: Multi-criteria analysis (MCA)

MCA is an alternative to defining monetary values for all the major costs and benefits when this is impractical. The DETR has developed a manual for the application of MCA to decision-making, entitled *Multi Criteria Analysis: A manual*.

MCA establishes preferences between options by reference to an explicit set of objectives that the decision-making body has identified, and for which it has established measurable criteria to assess the extent to which the objectives have been achieved. A key feature of

MCA is its emphasis on the judgement of the decision making team, in establishing objectives and criteria, estimating relative importance weights and, to some extent, in judging the contribution of each option to each performance criterion. One limitation of MCA is that it cannot show that an action adds more to welfare than it detracts.

There are a number of different MCA techniques some of which are of theoretical interest, but of little practical value and others of which yield fruitful applications. The DETR manual provides an overview of these different techniques and evaluates their potential application.

The theoretical literature alludes to the need for a systematic approach to cost benefit analysis and many authors call for government to develop ways of producing such analyses. As outlined above, there is substantial information on the methodological approach to cost-benefit analysis. What is lacking, however, is examples of the application of cost-benefit analysis or processes of identification and assessment of costs and benefits in the context of audit. Hood et al (1998) identify three elements to develop a more coherent system of oversight:³⁵

- A common set of principles in the form of a code of practice applying to regulators in government, which includes a systematic logging of the compliance costs they impose on their charges. They argue that there is a strong case for bringing the assessment of compliance costs for public sector regulation in line with the regime applied to business regulation.³⁶
- Systematic analysis of compliance costs and benefits.
- More coherent principles of investment in regulation within government.³⁷ That is, the ‘cost assurance function’ of the process – the extra assurance gained about the health of the system being regulated obtained by increasing investment in audit and inspection.³⁸ Argue that at present, resourcing of the regulators is wholly governed by happenstance and special pleading, and is not justifiable by any coherent investment criteria.³⁹

Hood and Scott (2000) argue that compliance costs are more tractable if defined in a narrow sense as what it costs regulatees to interact with regulators in providing information, arranging visits, co-ordinating and rehearsing responses etc, but not including costs of substantive policy or organisational changes.

³⁵ Hood et al (1998).

³⁶ Under the guidance for Regulatory Impact Assessment, regulators are required to assess both the policy and implementation costs of any regulatory proposal on businesses, charities and voluntary sectors. Implementation costs refer to the ‘red tape burden of regulation’ and includes, for example, legal and other consultancy fees associated with understanding the requirements of the regulation, staff costs or time in training staff for the familiarisation of new regulations or procedures, staff costs filling in forms associated with regulation, inspection and licence fees, costs associated with buying new equipment (for example, computer systems) in order to be able to comply with the new regulations, enforcement and implementation costs (for example, the costs arising from the need to devote additional time and resources to satisfying inspection officials), and time dealing with officials, keeping records and reading guidance. Policy costs are those costs that are directly attributable to the policy goal of the regulation.

³⁷ Hood et al (1998).

³⁸ Power, M (1997).

³⁹ Power (1997) argues that the cost assurance function is ultimately inscrutable as not only do practitioners not know the shape of the function, they do not know where they are on it or how to calibrate the assurance axis. As a result, there is no way of specifying the assurance production function independently of a practitioner’s own qualitative opinion process.

Power (1997) makes a case for evaluation rather than audit as the basis for establishing impact. He argues that the approach should be qualitative rather than quantitative – using social science techniques to examine the behavioural impacts, rather than seeking to measure the benefits directly, given the difficulties of the latter.

Boland and Fowler (2000) examine the use of influence diagrams and dynamic simulation to unravel effects of review and other performance improvement mechanisms.

Other thoughts

While it is necessary to safeguard public interest in cases of inadequate service performance and to provide an external discipline to councils to improve their overall performance, inspections ought to be proportionate to performance and public risk; and need to be balanced with increased resources for enhancing effectiveness, innovation and building leadership capacity.⁴⁰ It is argued that regulatory reform (for example, setting up the Public Sector Team within the Regulatory Impact Unit) does not extend its thinking beyond “reducing burdens” to think in any serious way about how to make oversight of the public sector more effective (as opposed to less burdensome). The question is are we focusing on the appropriate thing – assessing the costs and benefits of external review processes (aiming to reduce the red tape) or should we be evaluating the effectiveness of external review relative to other approaches, for example enhancing effectiveness through improved leadership or streamlining external review processes.

Broader measures to improve the effectiveness of external review specifically and public sector services in general include:

- Establishing fora for regulators in government to identify good practice and discuss general approaches and overall philosophy across the various domains of regulation. Government has established the Public Audit Forum for the audit bodies, and more recently the Best Value Inspectorate Forum for the inspectorates, but there is no discussion across the different types of external review bodies.
- Systematically exposing regulators in government to productive competition and rivalry. Argue that the response of the regulators to the overlap between them has been to collaborate rather than to compete, particularly with regard to the debatable lands lying between audit, professional inspection and funder-regulation. Argue that can introduce competition either through league table comparisons among regulators as a group and between regulators and their charges; or through systematic sunset- and market-testing of regulation in government; or through expansion of the scope for an element of choice of regulator by public service organisations.⁴¹
- Introducing randomness as a tool of regulation inside government (snap inspections and random scrutinies), especially at the top and centre of government where the social distance between regulator and the regulated body tends to be lowest and the risks of over-familiarity, therefore, highest.⁴² Argue that a way of keeping both the compliance and the administrative costs of regulation down is to use randomness in checking procedures. Advantages of random checking include the greater chance of breaking through information asymmetries through unannounced inspections or audits, the avoidance of pre-inspection stress, the reduced costs of limited sampling checks, the

⁴⁰ Quirk, B Blame and shame leadership *PubNet*.

⁴¹ Hood et al (1998).

⁴² Hood et al (1998).

reduced compliance costs for regulatees when inspectors visit them unannounced to view them in normal operation and thereby avoid the heavy costs (of document preparation, rehearsals, refurbishment of premises etc) often associated with long-heralded inspections) – some regulators already employ such tactics, eg Social Services Inspectorate and the Prisons Inspectorate.⁴³

Need to answer questions as to whether improvement and inspection are actually linked and if inspection does drive change, how does it do so? In what circumstances does inspection work best? What costs does it impose on the inspected bodies – in financial terms, in terms of disruption to ongoing service delivery and in terms of opportunity costs of staff time absorbed by the inspection process? What are the effects (both positive and negative) on staff morale? Need to develop a better understanding of whether, how and why inspection drives improvement and to evaluate the relative effectiveness of the different approaches being pursued by the multiplicity of unjoined up inspectorates that cover local government services.

The scale of inspection should be proportionate to risk. The proportionality of the response should be driven by an assessment of risk, for example, a body which has proved to be effective in managing itself may present a lower risk and require less scrutiny; and recognition that mistakes will be made, but should not be repeatedly made (resulting in a need for a degree of leeway for public managers taking risk). The more a body can demonstrate that it has successfully challenged itself to improve, the less inspection it should receive This is, however, a difficult principle, because it is not always possible to assess the risk until inspection is carried out.⁴⁴

There has recently been a spate of investigations into the role of audit and inspection and the balance between these regulatory functions and internal management. These reports reiterate some of the above questions and include:

- a survey by the Local Government Association of local authorities perceptions of inspection (*An inspector calls: A survey of local authorities on the impact of inspection*);
- a Performance and Innovation Unit report on *Better policy delivery and design: A discussion paper*;
- a Performance and Innovation Unit report on *Strengthening leadership in the public sector*.

The Local Government Association report found that local authorities agreed that “inspection plays a key role in the current approach to public service reform – with an emphasis on national performance indicators and targets, backed up with the threat of intervention where performance fails to improve.” However, “whilst there is widespread support for the principle of external inspection ... there are some legitimate issues to be explored:

- Inspections consume significant resources; does this represent the best value for money?
- Can the array of inspectorates be better joined up?
- How does inspection connect to improvement?”⁴⁵

⁴³ Hood, C, James, O and Scott C (2000)

⁴⁴ Audit Commission.

⁴⁵ Local Government Association (2001) *An inspector calls: A survey of local authorities on the impact of inspection*.

The survey found that local authorities generally recognised the value of inspection and considered external inspections to be an important element of service accountability and continuous improvement. Most of the respondents to the LGA's survey identified that inspections are very resource-intensive, particularly for local authority staff. Views on the ability of inspectorates to effect improvement were more mixed. While many believed that inspections can be a catalyst for improvement (74%), less than half the respondents felt that it had led to improvement.

The LGA survey states that there needs to be a new agenda with regard to inspection, including:

- a renewed clarity about the purposes of inspection – particularly its role in promoting good practice and supporting local authorities to improve;
- a fuller understanding of what drives organisational change and what delivers better outcomes – and of the contribution of peer reviews and support;
- a reconsideration of the focus and proportionality of inspection regimes – considering, in particular, outcomes for citizens;
- an exploration of the scope and potential for joined up inspection;
- consideration of the issue of quality assurance (including consistency and professional credibility).

The PIU report on *Better policy delivery and design* states “some of the current structures and cultures of audit militate against effective delivery: they are too focused on processes and rules rather than outcomes; too focused on micro-issues rather than strategy; and strongly skewed against entrepreneurship. In addition there is considerable evidence that the regulatory burden on some public service managers and front-line staff has grown unacceptably heavy. The Regulatory Impact Unit work on schools, police and GPs is already encouraging departments to think more seriously about the cumulative burden which results from inspection regimes and reporting requirements.”⁴⁶ They argue that “the fact that central government is accountable for results does not imply that it should specify how results are to be achieved. Too much central specification will tend to lead to demotivation, a failure to tailor services to local needs, and excess red tape ... there are some cases where such prescription is justified ... however, these periods of central direction should be relatively short – unless power and discretion are quickly passed back to front-line staff there is a risk of disempowerment and dependency.”⁴⁷ Government, therefore, needs to strike “the right balance between centralisation and decentralisation. It is conventional wisdom that the most effective organisations manage through objectives, not through detailed prescription.” The PIU argue that it would “be more meaningful for public accountability to rest more clearly with those genuinely responsible for delivery”, that is with Chief Executives, Chief Constables, head teachers etc rather than ministers. Further, they argue that leadership across the public sector needs to be promoted, strengthened and supported.

The PIU report on *Strengthening leadership in the public sector* recommends that there should be a better balance between freedom to lead and the ability to hold public service leaders to account for their performance. There should also be more intensive development of leaders and potential leaders, drawing on best practice, with a stronger emphasis on joining-up across sectors.⁴⁸ They argue that central government should think carefully about how it

⁴⁶ Performance and Innovation Unit (2001) *Better Policy Delivery and Design: A discussion paper*.

⁴⁷ Ibid.

⁴⁸ PubNet (2001) *Public sector drifting into leadership crisis*, Thursday, 29 March 2001.

defines tasks and rewards for leaders in the field and that inspection regimes could be more effective in holding leaders to account and in challenging them to improve their performance. They argue that targets can be used to help set outcomes, but if they are too rigid they can stifle initiative and innovation. There is a challenge, therefore, to strike the right balance between clear accountability, and giving leaders the freedom to take risks, or change course in order to better achieve the organisations goals. They argue that holding public sector bodies to account is necessary, but that arrangements for accountability and control can help or hinder leaders. Further, they state that it is usually more effective to define outcomes and objectives rather than to specify precisely how tasks should be carried out. Government has sought to follow this principle with the advent of Public Service Agreements and the principle is being established that good performance should earn greater freedom. They do not view freedom as an alternative to accountability, and accept that even the most effective leaders need to be challenged to improve their performance and held to account effectively. However, they argue that leaders who are overburdened with directions will be unable to function effectively. Arrangements for accountability must help to create the environment for leadership, so that, for example, appropriate risk-taking behaviour is not squeezed out. They argue that inspectorates need to do more to promote leadership. The effectiveness of leadership and management within hospitals, schools and local authorities are examined within the inspection frameworks, but leadership is often used as a catch all with the failings and successes of leadership often identified with those of the organisation. Inspectorates should help organisations to see more precisely the links between the quality of leadership and the effectiveness of service delivery and clarify what needs to change. They identify that within each sector, inspectorates already analyse thematic issues, such as leadership, primarily to inform future inspection frameworks; and argue that there would be considerable value in sharing learning about leadership across the range of inspectorates, since all have made criticisms in this area.

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Comparative examples

There have been changes to the inspection regimes that claim to reduce the burdens of inspection or audit on the regulated bodies. For example, while more activities are being subject to inspection (for example through the Better Value Inspectorate and the Commission for Health Improvement), across the different inspection regimes there has been a move toward a lighter touch model of inspection. This new model of inspection aims to introduce a risk-assessment approach to inspection which results in effective service deliverers receiving less rigorous inspection and channels resources toward the inspection of the weaker bodies. Changes to the inspection and audit regimes to reduce the burdens of the regimes on inspected or audited bodies appear to have been driven either from the bottom up, through lobbying or cumulative anecdotal evidence of the regulatory burdens collected through reviews (for example, newly announced changes to the inspection regime for higher education universities and colleges), or from the top down, through changes in Ministerial priorities. There have been no real hard studies of the costs and benefits of the different inspection regimes; and the impacts of the changes to the inspection regimes are yet to be evaluated.

To determine the expected benefits of inspection or audit regimes, one needs to look to the aims and objectives of those regimes. The examples below demonstrate that inspection and audit has dual roles of holding inspected/audited bodies to account (and thereby providing comfort/assurance) and contributing to the improvement of services (through promoting economy, efficiency and effectiveness in public service provision). The benefits accrued from both these roles are notoriously difficult to measure, as is discussed under the example of the Audit Commission.

While there is some anecdotal evidence suggesting the costs of inspection or audit to the regulated bodies, in particular those of OFSTED inspections, there is no real hard evidence of the costs of the different inspection regimes. In each case study area, allusions are made to the regulatory burdens of inspection/audit, including the resource-intensive nature of the regimes, the paperwork associated with the inspection process, and the limited usefulness of the process; but discussions and reviews of these regimes seldom go beyond identifying that there are costs to specify what those costs are.

The focus on performance analysis in the inspectorates, as with other public sector agencies, has been on cost-effectiveness of service delivery and efficiency improvements in resource use within the inspectorate itself. For example, OFSTED evaluate their performance in terms of a Service Delivery Agreement, the focus of which tends not to be on measuring the impacts (both costs and benefits) of inspection, but rather on meeting specific service and contracting targets. Other inspectorates also set performance indicators against which they measure and report on their performance. These performance targets also tend to lack any real analysis of contribution toward improving public services. However, there have been recent moves, for example by the Audit Commission, to include performance indicators which measure the contribution that regulatory bodies make to improvement. OFSTED have also included a draft indicator in their Service Delivery Agreement of the number of schools to improve since inspection.

In addition, the inspectorates tend to measure their cost-effectiveness in terms of their costs relative to the cost of the system as a whole (using this to justify rather than question the

inspection regime). So, for example, as the expenditure of the HMIC is 0.08% of the total cost of policing and the expenditure of OFSTED is less than 1% of the education budget, the inspection regimes are justified [erroneously?] on the basis that even if the benefits are small or not easily quantified, the costs are relatively so small that the inspection regime is warranted. Of course, this only includes the running costs of the inspection regime and does not include the costs to the inspected bodies. In addition, the DETR notes that the Audit Commission has not been subject to a VFM study by its auditor, the NAO, as it is perceived by the NAO to be low cost and low risk and, therefore, does not warrant such detailed audit.

The different regulatory styles appear to be key to the impacts of the different regimes on the bodies for which they are responsible. For example, the ‘name and shame’ approach adopted by OFSTED has been often criticised and is seen by some as having an extremely negative impact on teachers and the teaching profession. This may seem to be supported by the fact that there is a wealth of reviews, surveys and discussion around the impact of OFSTED in comparison to other inspection regimes. In contrast, for example, the collaborative style of the Social Services Inspectorate has been seen to be supportive and positive. It has been noted, however, that the true costs and benefits of these different regulatory styles have not been evaluated and, therefore, we cannot say whether, for example, the ‘adversarial’ name and shame approach of OFSTED provides more benefits than a more conciliatory approach or not.

Education

Office for Standards in Education (OFSTED)

The Office for Standards in Education (OFSTED), officially the Office of Her Majesty’s Chief Inspector of Schools in England, is a non-ministerial government department independent of the Department for Education and Employment (DfEE), which was established by the Education (Schools) Act 1992.¹

OFSTED’s remit is to improve standards of achievement and quality of education through regular independent inspection, public reporting and informed independent advice. In addition to the inspection of all maintained schools, OFSTED undertakes inspections of the Local Education Authorities (LEAs), 16 to 19 education, initial teacher training courses in universities and colleges, and other educational institutions in England. OFSTED is also responsible for inspection of publicly-funded nursery education, the inspection regime of independent schools, and the youth service and LEA-funded further education (including adult education). OFSTED is also responsible for providing the Secretary of State for Education and Employment with advice on educational matters. From September 2001, OFSTED will also be responsible for the regulation of childcare in England. This evaluative example focuses on OFSTED’s role in inspecting maintained schools, currently the major component of OFSTED’s work.

In order to understand the costs and benefits of OFSTED school inspections, one needs to look more broadly at the role and actions of other bodies involved in the OFSTED inspection process. For example, Local Education Authorities (LEAs), which have a primary duty to

¹ External inspection of schools was undertaken prior to the establishment of OFSTED and, in fact, goes back as far as 1839 when the first external inspections were undertaken by HM Inspectors of Schools.

raise standards in schools,² provide a range of support for schools, including in preparations for OFSTED inspections.³

Stated purpose of OFSTED

The Education and Employment Select Committee state that the OFSTED model and publication of comprehensive data about the performance of schools was predicated on the idea that the information produced by OFSTED should contribute to ‘a form of regulation by the market to encourage higher standards in schools ... the clear objective of the publication of league tables and so on is to use a kind of market mechanism to improve standards in schools.’⁴

The Education Sub-Committee of the Select Committee on Education and Employment states that “inspection provides information on the national state of education. It provides information on individual school’s performance to parents, the local community and the LEA, all of whom can use this information to hold the school accountable for its work. Inspection is thus partly an accountability mechanism. However, inspection may also be a tool for development of the institution concerned,” with schools being able to use the information as a starting point for further information.⁵

This highlights the dual roles of OFSTED inspection of, on the one hand, holding schools to account and, on the other, contributing to improvement.

The Select Committee for Education and Employment also identifies, however, that there is a tension between whether inspection is essentially for accountability or for direct improvement, raising the standards within the school.”⁶ Schools themselves are argued to vary in their perception of the role of OFSTED. Professor Maurice Kogan suggests that on the whole schools feel that external inspection by OFSTED is related to accountability of a particular kind of development.⁷

OFSTED’s stated aim is “to help improve the quality and standards of education through independent inspection and advice.”⁸

OFSTED’s stated objectives are “to deliver high quality inspection of schools, funded nursery education and LEAs, providing independent assessment to help the raising of educational standards; and to provide high quality advice, based on inspection evidence, to

² The contribution made by LEAs to the achievement of this target is monitored and evaluated by OFSTED and by the DfEE’s Standards and Effectiveness Unit.

³ Local Government Association (2000) *The LEA contribution to school improvement – A role worth fighting for*.

⁴ Select Committee on Education and Employment (1999) *Fourth Report: The work of OFSTED. Report from the Education Sub-Committee*.

⁵ Select Committee on Education and Employment (1999) *Fourth Report: The work of OFSTED. Report from the Education Sub-Committee*.

⁶ Select Committee on Education and Employment (1999) *Examination of witnesses, Wednesday 13 January 1999*.

⁷ Select Committee on Education and Employment (1999) *Examination of witnesses, Wednesday 13 January 1999*.

⁸ Ofsted (2000) *Ofsted’s corporate strategy 2000-01*.

the Secretary of State for Education and Employment to assist in the formulation and evaluation of Government policies.”⁹

In pursuing these objectives, OFSTED state that they intend to:

- carry them out efficiently, effectively and economically within the resources provided;
- work with their partners in education to raise standards;
- improve communications both internally and externally;
- value their staff and develop their potential.

It would appear, therefore, from OFSTED’s aims and objectives that it has a strong developmental role.

The inspection framework

Under the School Inspections Act 1996, a principal duty of the HMCI is to establish and maintain the system for the regular inspection by independent inspectors of all state-funded schools in England. Her Majesty’s Inspectors (HMI) are not themselves responsible for the inspection of the schools. Inspection is undertaken by independent registered inspectors who are contracted to undertake school inspections through a tendering process. OFSTED arranges for the initial and further training of these independent inspectors; keeps a register of those who have been approved to conduct inspection; keeps a roll of those who have been approved to work as a member of inspection teams; sets out requirements for the conduct of inspections; gives guidance on inspection and writing reports; monitors the way in which inspections are carried out to ensure that standards are maintained; and keeps the inspection system under review. This cadre of HMI are also responsible for providing the advice necessary to regulate and monitor the school inspection system; and visiting schools in order to report on good practice in teaching and management and issues such as public examinations and international comparisons. The HMI’s are also responsible for carrying out analysis to identify trends, evaluate the effects of educational policy, and follow up on issues and concerns to which inspection findings have drawn attention.¹⁰

All schools are required to be inspected at least once within six years of the end of the year in which their last inspection took place, with weak schools being inspected more frequently. The OFSTED inspection regime has been the subject of a number of changes since 1997.

Since September 1997, registered inspectors have had to indicate in their reports if a school has serious weaknesses; and since September 1998, OFSTED has been responsible for scrutinising and commenting upon the action plans of seriously weak schools and on the LEAs statement of action in support of the school. Those schools identified as weak have a year to overcome their weaknesses. OFSTED may visit to assess progress in the implementation of the school’s action plan, and lack of progress may result in the school being put into special measures or trigger an early inspection.

In September 1998, the Secretary of State announced that there would be a new and more flexible inspection regime in line with the Government’s policy of intervention in inverse proportion to success. The changes in the inspection regime took place in January 2000, with

⁹ Ibid.

¹⁰ Select Committee on Education and Employment (1999) *Fourth Report: The work of OFSTED. Report from the Education Sub-Committee.*

those schools which have proved most effective undergoing short inspections, whilst all other schools continue to receive full inspections. The inspection framework (as outlined in the document *Inspecting schools*¹¹) included other developments in school inspection:

- a reduction in the period of notice of inspection given to schools from at least one term to six to ten weeks;
- the principle of Best Value;¹²
- a greater emphasis on educational inclusion;
- the identification of underachieving schools, that is, those which do not require special measures, nor have serious weaknesses, but which are performing significantly less well than other schools of similar type;
- performance management in schools.

For full inspections, the inspectors will be in the school for one week. During the inspection, inspectors undertake observations of individual lessons, consider samples of pupils' work, talk to pupils, governors and school staff, and scrutinise the schools policies and procedures for different aspects of its work.

The most effective schools are selected for short inspection by reference to the following criteria: the quality of education as revealed by the previous inspection report; the trend in test/GCSE performance of the schools; and the standards achieved in test/public examinations compared to all schools in England and/or compared with similar schools. In short inspections, small teams of inspectors will spend two to three days in the school. They will not report in detail on each subject in the school. The summary reports will be similar for both short and full inspections, however.

OFSTED notifies the school of its inspection six to ten weeks in advance and asks the school's appropriate authority (in most cases this is the governing body) for key data to be supplied on Form S1.¹³ The information provided by the school is used by the contractor to form a team of inspectors with a range of expertise and experience to match the specification. The registered inspector will arrange a preliminary visit to the school to collect data and meet the head, staff and governors to discuss what they want out of the inspection and the results of the previous inspection. At this preliminary meeting, the inspector will request three forms (S2, S3 and S4), as well as "a small number of documents" which the school is expected to possess already.¹⁴ A meeting between the registered inspector and parents must also be arranged by the school.

Towards the end of the inspection, the registered inspector is required to consider whether or not the school is failing, or likely to fail, to give its pupils an acceptable standard of education and thus requires special measures; whether or not the school, although providing an acceptable standard of education, nevertheless has serious weaknesses in one or more areas of

¹¹ OFSTED (2000) *Inspecting schools: The framework*.

¹² Defined as 'a duty upon public bodies to deliver services to clear standards – covering both cost and quality by the most economic and efficient means available.'

¹³ Form S1 provides information about the school (eg pupil data, organisation and staffing).

¹⁴ Form S2 is used to collect factual information about the school relating to, for example, curriculum and finances. Form S3 asks the head teacher to state the extent to which the school fulfils its statutory requirements and to indicate the extent to which a range of monitoring and evaluation processes are in place. Form S4 provides an opportunity for the head teacher to contribute a structured personal statement to the inspection team.

its work; and whether or not the school, although identified as having serious weaknesses, is judged to be underachieving.¹⁵

After the inspection, the registered inspector produces a report which is given to the school to consider the final draft for factual accuracy (not to negotiate the findings). A report summary is provided to the parents of every registered pupil. Schools produce an action plan in response to the inspection report and present it OFSTED, parents and other necessary parties.

The findings of school inspections are published in league tables.

Evaluation of the impact of OFSTED

There is very little self-evaluation of OFSTED. Anecdotal evidence suggests that OFSTED, as well as the DfEE and the Select Committee for Education and Employment, do not question the need for independent inspection. For example, the Select Committee for Education and Employment, in their inquiry on the work of OFSTED expressed unquestioned “support for thorough, independent, external inspection of education services in England”.¹⁶

OFSTED’s evaluation of its performance is thus limited primarily to an assessment of its own cost-effectiveness. As part of the Modernisation Agenda, OFSTED has agreed to deliver services against specific targets and indicators (Public Service Agreement). The targets are intended to express either the **end results** that taxpayers’ money is intended to deliver, for example, improvements in educational achievement, or **service standards**, for example, smaller class sizes.¹⁷ The targets are intended to be specific, measurable, achievable, relevant and timed, relating to outcomes wherever possible. They aim to make it easier to measure and improve the public sector’s efficiency and thus raise its productivity (the quality and quantity of output delivered for the financial investment made). The Public Service Agreements (PSAs) aim to increase the accountability of government to Parliament and the public, enabling the identification of the effects of extra investment at the sharp end of public services; providing objective information to enable the public to make sure services are measuring up to what they want and need.¹⁸

OFSTED’s PSA states that it is to play a part in helping to achieve the Government’s wider objectives of raising productivity and promoting opportunity for all. The stated aims and objectives outlined above form part of OFSTED’s PSA. OFSTED’s PSA includes the following performance targets:

¹⁵ OFSTED *School inspections from January 2000*.

¹⁶ Select Committee on Education and Employment (1999) *Fourth Report: The work of OFSTED. Report from the Education Sub-Committee*.

¹⁷ Chief Secretary to the Treasury (1998) *Public service for the future: Modernisation, reform accountability*. HMSO.

¹⁸ Chief Secretary to the Treasury (1998) *Public service for the future: Modernisation, reform, accountability*. HMSO.

1999-2000 Performance Target	2000-2001 Performance Target
20% of schools to be inspected	18% of schools to be inspected
8000 nursery settings to be inspected	8000 nursery settings to be inspected
26 LEAs to be inspected	50 LEAs to be inspected
91% of inspection reports reviewed and monitored meeting HMCI's standards	92% of inspection reports reviewed and monitored meeting HMCI's standards
Target cost of contracted inspection: £54 million	Target cost of contracted inspection: £50 million
Initial Teacher Training: 200 secondary subject and 40 primary subject inspections in 1999/2000 academic year	160 secondary subject and 45 primary subject inspections in 2000/2001 academic year

OFSTED agrees to seek to carry out its objectives efficiently, effectively and economically within the resources provided.¹⁹ **Internal efficiency** will be measured by the following operational indicators: average time taken to handle all correspondence, average time taken to respond substantively to complaints about inspections and inspection reports, extent of achievement of the targets for prompt payments, and amount of competition for contracts measured by the average number of tenders per school. These indicators of OFSTED's performance do not appear to reflect the aims and objectives of the body. While they are constructed to measure internal efficiency, they measure neither end results nor external service standards.

OFSTED's Service Delivery Agreement for 2001-02 to 2003-04 reflects a shift in the type of indicators used and includes a draft indicator of the % of schools that have improved since their last inspection between April 2001 and March 2004.²⁰ This may provide data on OFSTED's contribution to school improvement, although it will be difficult to apportion improvements between internal school management and inspection.

OFSTED also has an efficiency target of reducing the ratio of running cost to programme cost by 2% from 2001-02 to 2003-04. The baseline for 2001-02 is 19.8%.

Her Majesty's Inspectors (HMI) monitor the quality of inspections by assessing the work of registered inspectors and their teams. After every inspection, schools are surveyed by OFSTED about their experience in order to help OFSTED to assess the quality of inspections and identify strengths and weaknesses in the process. A questionnaire is sent to all schools after their inspection to elicit views about the quality of the inspection and inspectors and the benefits that have been derived from inspection. The data gathered inform OFSTED's development of the inspection team.²¹ This information does not appear to be publicly available.

¹⁹ OFSTED's commitment to operating efficiently, effectively and economically within required guidelines and resources and in keeping with Government policies is to be achieved through, amongst others: resource accounting and budgeting which aims to ensure that the full economic costs of Government activities are measured properly, bring about improvements in the treatment of capital spending and require departments to report systematically on how their resources are allocated to their objectives; cost-effective services – OFSTED states that it is committed to the principles of Better Quality Services, seeking to ensure that functions are provided by the best supplier and that services are carried out by means of challenging, comparing, consulting, competing and collaborating. Besides contracting out school inspections, OFSTED contracts out a range of support functions in pursuit of cost-effectiveness; and corporate governance.

²⁰ OFSTED (2001) *Service Delivery Agreement 2001-02 to 2003-04*.

²¹ OFSTED (2000) *OFSTED's corporate strategy 2000-01*.

OFSTED is required to report to the Select Committee on Education and Employment on a regular basis. The Select Committee hears oral evidence from the HM Chief Inspector on an annual basis with regard to the HMCI's annual report. The Select Committee also holds regular meetings with the Chief Inspector, not only on his annual report, but also on the work of OFSTED itself.

The Select Committee of Education and Employment undertook a review of the work of OFSTED during the parliamentary session 1998-1999, publishing its report in June 1999.²² The starting point for their inquiry was based on "support for thorough, independent, external inspection of education services in England." The review took oral and written evidence from a range of interested parties, including university academics, teachers, head teachers, teacher trainers, school inspectors, contracting organisations for school inspections, school governors, the HM Chief Inspector of Schools in Wales, the former Chief Inspector of Further Education, the HM Chief Inspector of Schools in England, the Minister of State for School Standards and the Head of the DfEE's Standards and Effectiveness Unit. The findings of the report were broadly supportive of OFSTED's work although there were criticisms of the negative impact of a minority of inspection teams. It was argued that the level of stress in schools might be diminished if the normal period of notice of inspection was reduced to four weeks and that the inspection process might be enhanced if more account were taken of the school's own self-evaluation processes. The Committee's findings on the management style of the then Chief Inspector, Chris Woodhead, were critical. It noted its 'firmly held view' that the Chief Inspector's advice to Ministers and public commentary on education should be backed up by actual inspection evidence. OFSTED was not thought to have been successful seeking balanced media coverage of its work. It was recommended that in carrying out his role the Chief Inspector should be concerned to improve morale and promote confidence in the teaching profession.²³

An independent evaluation on OFSTED's system of inspection was commissioned by OFSTIN and presented as evidence to the House of Commons Select Committee in 1999. This research was undertaken by the Centre for the Evaluation of Public Policy and Practice, Brunel University. The report identified certain strengths in the system. The inspection framework was seen as promoting improved management systems and could be used as an aid to self-development. The inspection process was systematic, applied to all schools and could be a positive catalyst for change. On the other hand, the process was criticised because the summative judgements tended not to promote reflective professional development in schools and to be intolerant of alternative approaches to school effectiveness. The report summarised the implications of its research for policy and practice in inspection:

- an achievement of the OFSTED system of school inspection is that it has promoted acceptance of a culture of inspection;
- current inspection arrangements make too heavy workload and associated emotional demands on school personal;
- the costs, financial and otherwise, are not seen as value for money in terms of either school performance or pupil achievement;
- the system is seen as punitive and adversarial and not contributing to formative professional or school development (on the contrary, it is leading towards a form of dependant infantilism within the teaching profession);

²² Select Committee on Education and Employment (1999) *Fourth Report: The work of OFSTED. Report from the Education Sub-Committee.*

²³ Blake, D *British perspectives on the inspection of Initial Teacher Education.*

- contracting out to competing, peripatetic, journeymen inspectors does not produce the interaction between professionals required for continuing school improvement because informed reflective professional dialogue is based upon accumulated knowledge, expertise and the dissemination of good practice – the case for an established cadre of inspectors is made;
- there is a range of policy and practice implications for national government, OFSTED, schools, local authorities, parent and Governor associations, and teacher associations. Inspection should be more developmental in its mode of operation with strong elements of self-evaluation and peer review.²⁴

The Public Sector Team of the Regulatory Impact Unit was established in 1999 to look specifically at minimising the regulatory impact of central government on the public sector, and reducing or removing red tape and bureaucracy. The Public Sector Team undertook, jointly with the DfEE, a review of red tape in education entitled *Making a difference: Reducing school paperwork*. Schools were visited to see and hear directly how administrative work can get in the way of raising standards in the classroom. Key outcomes of the project included:

- OFSTED to test ways of using Annual School's census data to reduce the information schools need to fill in for themselves on Forms S1 and S2;
- OFSTED to provide guidance on how much information is needed on Form S4 and parts of Form S1;
- 2000 Autumn Package reduced in size by 50% and made available in CD-ROM format, alongside OFSTED's Performance and Assessment Report.

The research informed subsequent meetings and negotiations with key stakeholders, such as LEAs, OFSTED, the QCA and the TTA. The report focuses on outcomes and wherever possible, these have been quantified in terms of estimated hours that will be saved. Areas covered:

- *Universal document classification system*: Schools, head teachers and teachers receive documents from a number of bodies within the education sector – eg, DfEE, LEAs, OFSTED, QCA, TTA, the General Teaching Council. The documents differ considerably – in length, subject matter and purpose – from substantial guidance documents to single-page requests for information. Volume of material is an issue for head teachers and while they feel that much of what they receive is important and useful, they were concerned that too often the documents were unclear as to their purpose, the target audience, the action required, the timescales involved etc. Proposed introducing a universal document classification system which is estimated to save 1.8 million hours per year.
- *OFSTED pre-inspection forms (S1-S4)*: OFSTED sends forms S1-S4 to a school before an inspection takes place. Schools provide data to a variety of bodies and some of the data are similar, if not identical, to those requested by OFSTED. The DfEE and OFSTED have worked together to reduce that duplication. OFSTED is also playing a key role in the development of a Common Basic Data Set, which will, once introduced, provide OFSTED with much of the pre-inspection data it needs. OFSTED is also working with the Audit Commission and DfEE on the development of a consistent financial reporting framework for schools. Forms S1 and S2 require schools to provide some information that has already been or will be provided by the schools to DfEE (via the Annual Schools' Census) and LEAs. The information may not always be identical. Form S4 and some parts of S1 also request comments from head teachers without indicating how much

²⁴ Blake, D *British perspectives on the inspection of Initial Teacher Education*.

information is expected. This leads to some head teachers providing irrelevant information or far too much detail. The report suggests that the DfEE should provide OFSTED with Annual Schools' Census data to an agreed format and timescale. OFSTED will then test in 2001 how this data can be used to reduce the information that schools have to fill in for themselves on Forms S1 and S2. Head teachers would, of course, have the opportunity to check the data for accuracy. OFSTED should also provide head teachers with guidance on how much information is needed on Form S4 (and parts of Form S1) for 2001/2 inspections. It is suggested that the benefits of these changes can be estimated at 3,000 hours per year.

- *Autumn Package*: The Autumn Package of Pupil Performance Information is sent to schools every October to assist them and their governing bodies in reviewing school performance and informed, challenging future targets. It enables them to calculate and compare pupil performance with national trends and with performance of other schools; and individual pupil progress with national pupil progress between Key Stages. OFSTED's Performance and Assessment (PANDA) Report is an integral part of the Autumn Package, but was previously sent to schools in March. The PANDA demonstrates each schools performance data in comparison with both national averages and with other schools in similar contexts. The size of the Autumn Package has been reduced in size by over 50% and made easier to use. OFSTED's PANDA was issued close to the rest of the Autumn Package to remove duplication. Every school has received a CD-ROM version of the Package, which will automatically plot school against national progress when loaded with school data.

Regulatory burden: Costs and benefits of inspection

Ofsted state that it "strives to ensure that the burden of inspection on schools and teachers is kept to a minimum consistent with the aims and needs of inspections. Short inspections and shorter notice for all schools are helping to reduce that burden. With the exception of the standard forms, the documentation required by inspectors is limited to what schools would normally expect to be available."²⁵

The Education Sub-Committee of the Education and Employment Select Committee states the "key test of effective inspection is the extent to which it enhances the education of the children."²⁶

The Public Sector Team states that "for a process to be beneficial and non-bureaucratic, the outputs should at least equal the inputs and ideally exceed them."²⁷

Benefits

Anecdotal evidence suggests that the benefits of OFSTED inspections include:

- it reinforces the culture of evaluation in schools;
- it has had particular effects in the enforcement of what the management of schools and the acceptance of the need for an objective set of targets and assessment of pupils (the objective styles of evaluation);

²⁵ Ofsted (2000) *Ofsted's corporate strategy 2000-2001*.

²⁶ Select Committee on Education and Employment (1998/99) *Fourth report: The work of OFSTED. Report from the Education Sub-Committee*.

²⁷ DfEE and Cabinet Office *Making a difference: Reducing school paperwork*.

- parents appreciate the fact they are given external judgements which were not easily available to them before.

The Education and Employment Select Committee identify that inspection framework was widely praised in evidence to their enquiry as a valuable tool for school development and self-evaluation. Schools use the OFSTED inspection framework to evaluate their own practice and many find it a useful tool for doing so. The process of inspection itself, however, had more mixed reactions.

The National Association of Governors and Managers have argued that OFSTED, through its existence, has empowered governing bodies, enabling them to gain entry into legitimate area of concern which otherwise would have been closed to them.

The verdict is out as to whether OFSTED has achieved the development which it was set up to deal with and/or whether schools themselves recognise that OFSTED inspection is purely about accountability or is indeed developmental. In their review of the *OFSTED system of inspection*, Beale et al have looked at the extent to which OFSTED's claim to contribute towards development and improvement of education is valid. They argue that it is a very difficult point to unravel and that schools would say that they believe inspection should take place, but would prefer different systems for it.²⁸ Professor Maurice Kogan states that there is no real hard evidence data about OFSTED and its impact on standards or school performance. He argues that "the really difficult issue remains making a judgement on how far such a major system as OFSTED has an impact on such complex activities as what goes on in schools." Professor Maden states that one needs to "understand the wider context of the way in which educational organisations can be properly and rigorously evaluated."

Costs

The Education and Employment Select Committee allude to the costs of inspection, stating: "Inspection is for many schools, a stressful experience. We were provided with examples of inspections which had negative effect on teachers and the schools. This, we have no doubt, has contributed to what one of our witnesses described as the 'demonisation' of the OFSTED process. We recognise the seriousness of these cases, but note that the majority of schools found their inspection teams to be professional and courteous."²⁹ They argue that a reduction in the period of notice of inspection which is provided to schools to four working weeks would benefit schools as it would reduce the time for schools to assemble unnecessary and irrelevant masses of paper and also reduce the amount of time teachers have to develop 'anticipatory dread' of the forthcoming inspection." The impact of the reduction in the notice period has not been publicly evaluated.

The Education and Employment Select Committee also allude to the costs of preparation for inspections. They argue that many schools over-prepare for the inspection, using LEA advisors, inspectors and other consultants to undertake a full or partial review of their activities and prepare large amounts of paperwork in advance of inspection. Some witnesses to the Select Committee state that the large amounts of paperwork identified by governors as

²⁸ Select Committee on Education and Employment (1999) Minutes of Evidence of examination of witnesses: Professor Maurice Kogan, Professor Margaret Maden, Ms Sandra Jones and Ms Valerie Beale, Wednesday 13 January 1999.

²⁹ Select Committee on Education and Employment (1998/99) *Fourth Report: The work of OFSTED. Report from the Education Sub-Committee.*

being a major cost of inspection were, in fact, self-generated and not required by the inspection process.

The Education and Employment Select Committee also found evidence to suggest that preparation for inspection interferes with normal school development work and impaired teaching effectiveness. Many schools stayed open during holidays and weekends to allow teachers to prepare for inspection.

The evidence presented to the Select Committee also showed differences in views between headteachers and teachers on the one hand and governors and parents on the other. For example, almost all governors felt that school accountability had been improved as a result of the OFSTED system, whereas virtually no headteachers and teachers agreed with this view. Parents felt reassured by the OFSTED process and felt that OFSTED would have an impact on national standards. Evidence also suggested that headteachers felt that inspection reports were fair and valid and the key issues were seen as being fair and relevant to most heads, parents and governors. However, the reports were not seen to be telling the schools anything new and the action plans drawn up in response to OFSTED reports were seen mainly as a formality.³⁰

Furthermore, they note that the regulatory style of the former Chief Inspector of Schools, Chris Woodhead, may contribute to the demoralisation of teachers. They stated that there is a “widespread perception that some of Mr Woodhead’s views are based more on his opinions than on inspection evidence.” They argued that the Chief Inspector should adopt a more conciliatory approach, should be concerned with improving morale and promoting confidence in the teaching profession, and should limit his commentary on education to that which can be backed up by inspection evidence gathered by OFSTED.

Others have also focused on the regulatory style of OFSTED. Travers (2001), for example, states that Chris Woodhead was perhaps more visible than virtually all the other inspectors and auditors put together, arguing that “Woodhead and his teams stalk the land, bringing fear and retribution to those suspected of wrongdoing.”³¹ The style evolved by Woodhead was perhaps the definitive version of a brutalised naming-and-shaming model of inspection. Woodhead is perceived as “having set a gold standard for inspectorial beastliness. His departure raises the question of whether his full-throttle assault on what he saw as failing teachers, school and local authorities was (and is) the best approach for getting poorly performing public services to function more effectively.” Many commentators believe that the Woodhead doctrine demoralised teachers, driving down standards and discouraging new recruits into the profession. Others are convinced that, without a forthright attack on lazy and incompetent vested interests, many pupils would have continued to be educated in ways that reinforced under-achievement. Travers argues that an evaluation of these different regulatory styles is required to determine the actual impacts. The IPPR argue that the failure of inspected bodies to use inspection as an opportunity to challenge and improve on current practice is aggravated when inspection over-emphasises naming and shaming. They argue that naming and shaming may be effective in highlighting areas of poor performance, but does little to motivate organisations to improve. The IPPR states that inspected bodies will not own the findings of inspection unless they are perceived to be fair and strike the right balance between praise and criticism. They argue that where the legitimacy of inspection is undermined, the

³⁰ Select Committee on Education and Employment (1999) *Fourth Report: The work of OFSTED. Report from the Education Sub-Committee.*

³¹ Travers, T (2001) *Where now for the watchdogs? Public Finance.*

reaction is likely to be 'compliance' behaviour, with organisations becoming skilled in passing inspections, rather than translating the results of inspection into improvement in service performance.³²

The Education and Employment Select Committee also identified a key weakness of the inspection framework as being the practice of reporting school outcomes against national norms for educational achievement. They identified this as being a factor which could lead to 'disillusionment' in some schools.

The report *Review of the OFSTED system of inspection* by Beale, Jones and Kogan attempts to cost the OFSTED inspection process. Their report includes the costing of the following elements:

- the cost of OFSTED's school inspection programme (the overall figure for OFSTED in 1999 was £150 million, including its other services, which amounted to less than 1% of the education budget);
- the cost of LEA's – the amount of money from the LEA budget, excluding the standards fund, to go in and work with schools primarily before the inspection takes place (that is, LEA expenditure supporting school inspection when OFSTED is involved in inspecting schools);
- the cost to schools as a proportion of the budget over which they have control.

They state that the costs of OFSTED are high when comparing them with other evaluative bodies in England and elsewhere in the UK and are also high for the schools and for the local authorities. The criticisms of OFSTED centre primarily on the change model implicit in the work that it does and the way that it does it. While heads may feel the total judgements to be fair, the experience is generally believed to be punitive and unproductive because it is not tied up with a process of development. Similar criticisms are not made of other national bodies, such as the SSI and the Audit Commission.

A recent newspaper report suggests that there are also behavioural costs attached to OFSTED inspections. The article states that head teachers have been accused of 'playing a game' to win pupils higher grades and push their schools up the league tables by challenging thousands of GCSE and A-level results. The article argues that the move is paying off, with twice as many GCSE results being upgraded on appeal in 2000 than in 1999, and the number of mark-ups on A-level papers increasing by a third.³³

Value-for-money?

The Education and Employment Committee argue that the cost of OFSTED in relation to the education budget amounts to less than 1% and that "maybe that is a reasonable cost for changing the culture and, as we have agreed, clearly bolstering the role of the head in developing the school."³⁴

³² IPPR *Delivering change, supporting change: The role of inspection in improving public services – a discussion paper*.

³³ *The Times*, GCSE pupil mark up exam appeal success, Tuesday March 27, 2001.

³⁴ Select Committee on Education and Employment (1999) Minutes of Evidence of examination of witnesses: Professor Maurice Kogan, Professor Margaret Maden, Ms Sandra Jones and Ms Valerie Beale, Wednesday 13 January 1999.

Quality Assurance Agency for Higher Education (QAA)

The QAA was established in 1997 to provide an integrated quality assurance service for UK higher education institutions. The QAA is an independent body funded by subscriptions from universities and colleges of higher education and through contracts with the main funding bodies, such as the Higher Education Funding Council.

Role of the QAA

The QAA's core business is to review the quality and standards of higher education universities and colleges. It does this by auditing institutional arrangements for managing quality and standards, and by assessing the quality and standards of teaching and learning at subject level. These activities result in reports that are available to the public, as printed publications and on the Agency's website.

The QAA's mission is to promote public confidence that quality of provision and standards of awards in higher education are being safeguarded and enhanced. The QAA states that it does this by:

- working with higher education institutions to promote and support continuous improvement in the quality and standards of provision;
- providing clear and accurate information to students, employers and others about the quality and standards of higher education provision;
- working with higher education institutions to develop and manage the qualifications framework;
- advising on the grant of degree awarding powers and university title;
- facilitating the development of benchmark information to guide subject standards;
- promulgating codes of practice and examples of good practice; and
- operating programmes of review of performance at institutional and programme levels.

The main purposes of QAA assessments are stated to be:

- to secure value from public investment, by ensuring that all education for which funding is provided is of approved quality, and by encouraging speedy rectification of major shortcomings in the quality of education, and to enable judgements to inform funding should the funding council so decide;
- to encourage improvements in the quality of education through the publication of subject review reports and subject overview reports, and through the sharing of best practice;
- to provide, through the publication of reports, effective and accessible public information on the quality of HE.

The inspection framework

The method and procedures of inspection focus on the establishment, maintenance and enhancement of academic standards. These are matters for which the primary responsibility lies with the HE institution. However, the funding councils have a statutory responsibility to secure that provision is made for assessing the quality of education they fund. The QAA, therefore, acts on behalf of the funding bodies in this respect.

The QAA aims to provide information that is objective and independent by:

- reporting on programme outcome standards: concerned with the appropriateness of the intended learning outcomes set by the subject provider (in relation to relevant subject benchmark statements, qualification levels and the overall aims of the provision), the effectiveness of curricular content and assessment arrangements (in relation to the intended learning outcomes), and the achievements of students;
- reporting on the quality of learning opportunities in a subject: concerned with the effectiveness of the teaching, the learning resources and the academic support in promoting student learning and achievement across the various programmes in the subject area;
- reporting on institutional management of standards and quality: concerned with the robustness and security of institutional systems relating to the awarding function. This involves, in particular, arrangements for dealing with approval and review of programmes, the management of institutional credit and qualification arrangements, and the management of assessment procedures.

The overall process of gathering evidence about standards and quality is aimed to be effective and efficient and avoid, as far as possible, duplication of effort.

Academic review aims to be a dynamic engagement with the internal processes of an institution over a six-year cycle. Subject review updates continuously the picture that the QAA has of an institution, and provides audit trails to inform judgements about overall institutional systems. Institutional review thus aims to be a continuous process, with each subject review contributing information to the overall picture. That picture helps determine the intensity of scrutiny needed to report reliably in subsequent subject cycle reviews, and to make summative judgements on overall institutional systems once in each cycle.

For both subjects and institutions, the methods of academic review are centred on self-evaluation documents produced by the institution. Academic reviewers test, by means of their own observations and analyses, the statements made by institutions in their self-evaluation documents. Secondly, they make judgements on the appropriateness and effectiveness of the provision.

Evaluation and change in the inspection system

Inspection in higher education universities and colleges is highly topical featuring strongly in news headlines of late. The Education Secretary, David Blunkett, recently announced that the inspection of teaching in universities would be drastically reduced. Under these proposals, universities that score well in regular reviews will be exempt from the next round of inspections – except for a random sample.³⁵ Exempting departments scoring top marks from future scrutiny will result in a 40% reduction in the number of inspections taking place. While the QAA had proposed to implement a new lighter touch inspection regime in 2002, the announcement by David Blunkett pre-empts this, providing even lighter touch inspection than proposed. This has resulted in a heated debate, involving the QAA (responsible for the assessments), student leaders (who think that students need the information and that the assessments ensure quality), and academics (who have been complaining for some time of the red tape resulting from over-inspection and for whom the recent announcement to reduce inspection was “calculated to please”).³⁶

³⁵ *Financial times*, High-scoring universities may be exempt from inspection, Thursday March 22, 2001.

³⁶ *The Independent*, Lightly does it for higher education, Thursday 5 April 2001.

John Randall, Chief Executive of the QAA, has stated “It is important that public information continues to be available to support strategies such as widening participation in higher education for low-income families. Research has shown that students from backgrounds that don’t have networks of contacts with personal experience of higher education have a greater need for independent information about quality and standards.”³⁷

The universities complaint is that they are groaning under the weight of bureaucracy of all kinds – teaching quality assessments, institutional audits, the research assessment exercise and teacher-training inspections. The total cost of all this has been put at £250 million in paperwork and staff time. The LSE’s assistant registrar stated “it’s clear to us that the costs of these exercises hugely outweigh any benefits. Over the past two years, the QAA has introduced a number of initiatives that are antithetical to the idea of higher education as we see it. It’s too prescriptive and detailed, taking away our scope to regulate our own affairs in key academic areas.”³⁸ The 20 top universities were not pleased with the new lighter touch programme that has been proposed by the QAA because it includes a list of requirements – subject benchmarking statements, programme specifications and a code of practice. Under the new lighter touch programme, already in place in Scotland, universities would be rated for whether they are failing, approved or commendable in three areas – teaching and learning, student progression and learning resources. In addition, any exemplary features will be described. The Scottish Experience is argued to have demonstrated that the new lighter touch system is not much lighter touch, and the universities have expressed concern that there will be a tendency to compete on the basis of exemplary features. “Universities want to see the money saved – which is thought to include up to £25 million in red tape – to ease what they have called a crisis in the funding of the sector.”³⁹

There have been a number of issues leading to the state of inspection of higher education universities and colleges coming to a head. These include increasing complaints within the universities about the usefulness of the QAA in achieving its targets with, for example, the LSE considering seceding from the QAA and lobbying for another quality assurance system (although funding depends on the QAA and, therefore, it is unlikely to do so) and King’s College London claiming a failure in the QAA’s process of institutional audit resulting in no added benefits of audit. Primarily, however, reports suggest that the process of change in the inspection regime for higher education universities and colleges has been a political one, with representations being made directly to the Prime Minister and his education adviser. In addition, there has been an accumulating response to this high profile lobby within the House of Lords, the Education Select Committee and in the opposition.

Policing

Her Majesty’s Inspectorate of Constabulary (HMIC)

The HMIC is an independent inspectorate located outside the tripartite policing structure (that is, the Home Secretary, police authorities and forces), although it works closely with the three parties. The HMIC is funded by central government through the Policing and Crime

³⁷ Ibid.

³⁸ Ibid.

³⁹ *Financial times*, High-scoring universities may be exempt from inspection, Thursday March 22, 2001.

Reduction Group of the Home Office. Expenditure is controlled by government accounting rules.

In addition to the HM Chief Inspector of Constabulary (HMCIC), there are four HM Inspectors based in regional offices and one from a non-police background to focus specifically on police training. Each Inspector has a small team of staff officers and support staff to assist in inspections. Inspectors conduct formal inspections of the forces in their regions and produce public reports. They also visit for other reasons, including to further the professional relationship with the Chief Constables and police authorities. Inspectors also inspect various police forces, outside of England, Wales and Northern Ireland, by invitation, reporting to their representative authorities.⁴⁰

The HMCIC co-ordinates the work of HM Inspectors and advises the Home Secretary on professional policing matters. The HMCIC is supported by police officers seconded from forces and civil servants based in the Home Office. In addition, there are seven Assistant Inspectors, including five from a non-police background who add an external perspective to inspections. Two of these Assistant Inspectors focus specifically on race and diversity issues.

Role of HMIC

The role of the HMIC is defined in the Police Acts (1994 and 1996), which allow it to report to the Home Secretary on the efficiency and effectiveness of the 43 police forces in England and Wales, and the Local Government Act 1999, which relates to Best Value and has widened the powers of the HMIC to include the inspection of police authorities. The HMIC states that it is responsible for examining the efficiency and effectiveness of the police service to ensure that it is contributing to the Ministerial priorities of policing.⁴¹ It undertakes inspections of police performance with the objective of measuring how forces are performing against Ministerial priorities and national standards to encourage high quality, significant improvement and to identify good and poor performance.

Statement of purpose: “To promote the efficiency and effectiveness of policing in England, Wales and Northern Ireland through inspection of police organisations and functions to ensure:

- agreed standards are achieved and maintained,
- good practice is spread; and
- performance is improved.”⁴²

Also to provide advice and support to the tripartite partners and play a role in the development of future leaders (that is, the HMIC provides advice on all senior appointments and encourages the development of talent within the police service).

The HMIC, therefore, has very clearly stated functions of, on the one hand, ensuring that a minimum level of quality of policing is maintained and, on the other, contributing to the improvement of policing through, for example, spreading good practice.

⁴⁰ HM Inspectorate of Constabulary (2000) *A strategy for excellence: April 2000 – April 2003*.

⁴¹ HM Inspectorate of Constabulary (2000) *A strategy for excellence: April 2000 – April 2003*.

⁴² *Report of Her Majesty's Chief Inspector of Constabulary 1999/2000*. HMSO.

The inspection process

A new diagnostic model of inspection was introduced in April 2000, taking a risk assessment approach to inspection. The model is “a structured methodology to analyse, assess and score forces’ performance against a number of protocols (statements of good practice in operational and organisational activities)” which analyses performance to allow the HMIC to judge the level of inspection needed. Under this model, poorer performing forces receive more inspection attention than successful forces. This differs from the previous model where every force received a comprehensive inspection every 18 months regardless of performance. The new inspection model focuses on outcomes and measures performance against a number of protocols, all of which are linked to Ministerial priorities and objectives for policing and include Best Value indicators.⁴³ The inspection of forces results in the production of reports which include recommendations and professional advice with the aim of helping develop the thinking of police forces in improving effectiveness.

The HMIC also undertakes inspections of police training with the objective of ensuring that police training is effective and efficient. This includes inspection of police training establishments, comment on training within police forces, advice on best practice and Best Value.

The HMIC also undertakes thematic inspections, with the objective of helping the police service to achieve the Ministerial priorities for policing, including improving police performance in areas of crime reduction and good community and race relations. Thematic inspection reports have included foci on racial discrimination in policing (“Winning the Race”), recommendations to help forces achieve value for money (“What price policing”), ways in which integrity can be monitored and enhanced (“Police integrity”), crime reduction (“Beating crime”) and police training (“Managing learning”). Thematics are seen by the HMIC as an effective way of identifying and spreading good practice.⁴⁴ Furthermore, thematic inspections are seen by the HMIC to enable the Home Secretary, police authorities and Chief Constables to identify issues which need to be addressed in order to raise police performance. Thematic inspections are followed up to see how forces are taking on recommendations.

Other areas of work include working with other agencies, which have an interest in the delivery of police services, to avoid unnecessary duplication and overburdening of forces and police authorities with inspection (for example, Audit Commission and Home Office in delivery of Best Value; SSI; Youth Agency; HM Fire Services Inspectorate; HM Inspectorate of Prisons; and HM Inspectorate of Probation).

The HMIC collects data on police performance to inform inspections and identify areas of good practice and possible weaknesses. This data measures performance of police forces against key performance indicators set by Ministers. This data is provided by the forces either directly to the HMIC or to the Home Office Research, Development and Statistics Directorate.

⁴³ *Report of Her Majesty’s Chief Inspector of Constabulary 1999/2000*. HMSO.

⁴⁴ HM Inspectorate of Constabulary (2000) *A strategy for excellence: April 2000 – April 2003*.

Evaluation of costs and benefits

There is little evidence of the evaluation of costs and benefits of inspection by the HMIC and inspection appears to be given an intrinsic value (that is, inspection is unquestionably seen as good and necessary).

The HMIC do, however, allude to the burdens of inspection through a number of statements and actions reporting to reduce such burdens. For example, there has been a gradual reduction in the intensity of the inspection regime, moving from annual inspections, to an inspection every 18 months, and finally to the risk assessment, diagnostic model outlined above (that is, inspection inversely proportionate to performance). With reference to the new approach to inspection of police forces, the HMIC state “this is a very different approach. Up until now inspection has tended to cover all areas of policing activity, delivering a stock service regardless of performance. This new way of working will allow us to reduce the burden on forces, target our activity more effectively and optimise our resources.” Furthermore, they state “in April 2000, HMIC introduced a new risk-based model of inspection, aimed at reducing the burden on forces and focusing inspection so that we are able to look in more detail at areas of good and poorer performance.” While the HMIC reports to have adopted the new risk-assessment model after reviewing its previous [burdensome] inspection regime, there is no evidence to suggest that the burdens of the previous inspection regime were, in fact, either qualitatively or quantitatively evaluated. Rather the shift in approach is likely to be in response to the Government’s Modernising Agenda which proposes lighter touch inspection, or inspection inversely proportionate to success.

With regard to thematic inspections, the HMIC indicate that they are aware of the burdens of following up such inspections, stating “The volume of thematic work over recent years placed an unacceptable burden on individual force inspections to chase progress. A changed approach was devised in 1998 whereby the regional HM Inspector monitors progress in correspondence with each chief constable. The latter forwards action plans and position statements to the regional office and the effectiveness of implementation is assessed during subsequent inspections. This approach has proved a significant improvement in maintaining the threshold of accountability.” The focus here is, however, on reducing the burden on the Inspectorate rather than the inspected.

The HMIC does review its own cost-effectiveness, although this is not evaluated against its role or outcomes. The HMIC presents its annual running costs and evaluates their cost-effectiveness in terms of its costs relative to the total funding made available to the police service in England and Wales, benchmarked against other inspectorates. In 1999/2000, total HMIC expenditure was £5.49m or 0.08% of total police expenditure (£6,943m). The HMIC stated “benchmarking exercises with other inspectorates have demonstrated that HMIC provides a most cost-effective service.” This does not look at the costs and benefits of inspection, but rather implies a presupposition that inspection is sufficiently beneficial and warranted given the relatively small costs to Government. It only looks at part of the balance sheet.

Another way in which the costs are evaluated are in terms of efficiency gains, compared annually. The HMIC assesses its reductions in real costs to deliver the same or similar inspection service on an annual basis.

On the other side of the balance sheet, the HMIC does follow up on thematic inspections, evaluating progress in terms of implementation of recommendations. As part of its inspection process, the HMIC also measures performance improvements in police forces. While it may be possible to attribute benefits (or improvements) from certain recommendations made in relation to thematic inspections to the inspection process, the apportionment of improvements resulting from police forces inspections (as compared with internal performance management) may prove more difficult.

The most glaring omission is the lack of any substantial analysis of the costs of inspection to the inspected bodies (authorities, forces and training agencies). While there are anecdotal references to inspection burdens to the forces, and subsequent changes to the inspection regime to reduce those burdens, there does not appear to be any actual evaluation of compliance costs, behavioural costs or such like.

External evaluation of the HMIC

The HMIC reports very infrequently to the Home Office Select Committee. The HMIC has not presented oral evidence to the Select Committee since 1998, where it was a witness to a review of police training initiatives. There has been no review of the work of the HMIC by the Home Office Select Committee, apart from as an expert witness in the Select Committee's enquiry on police recruitment and training. Unlike the case of OFSTED, the annual reports of the HMIC do not appear to be discussed by the Select Committee.

The Association (ACPO) states: "Measuring police performance is at the heart of public accountability. The [ACPO Performance Management] Committee has been making significant progress to ensure that measurement of police effectiveness is based on sound data and reflects the capability of the Service to deliver." They argue that "... the Police Service has faced a plethora of different and sometimes contradictory initiatives. It has been the task of the Performance Management Committee ... to try to discern some strategy or broader picture from the welter of performance measures, indicators and new requirements for planning and inspection." They state that they are "working to define performance indicators so that they match more closely the realities of operational policing and, where they are intended to act as measures of comparison of force performance, represent targets which are realistically attainable."

Personal Social Services

Social Services Inspectorate (SSI)

The SSI was set up in 1985 as a professional division within the Social Care Group of the Department of Health. The SSI assists Ministers in carrying out their responsibilities for personal social services and exercises statutory powers on behalf of the Secretary of State for Health. The personal social services help people of all ages and with a variety of needs. Services include social work, residential and day care, and help in the home. The work of the SSI is undertaken through:

- Social Care Regional Offices which help local councils to implement the Government's social care policies and monitor their performance;
- Inspection groups who regularly inspect the quality of aspects of social services in each local council;

- the SSI/Audit Commission joint review team who assesses how well each local council with social services responsibilities serve their population;
- inspectors based in the Department's policy branches who provide professional advice and expertise to Ministers and policy-makers.

The SSI consists of a Chief Social Services Inspector, two Deputy Chief Inspectors, an Inspection Division including six inspection groups and an inspection resources group, four regional offices of Social Care Groups managed by Assistant Chief Inspectors, and the SSI/Audit Commission Joint Reviews.

The Inspection Division is a core component of the SSI and is responsible for inspecting the quality of personal social services provided by local authorities and some independent organisations. Where responsibilities are shared, it also carries out inspections with other central government inspectorates, such as education, police and probation. With the Audit Commission, it carries out joint reviews of social services authorities in England.

Role of the SSI

The annual report of the SSI does not illuminate either the mission statement of the SSI or its objectives in any coherent manner. However, the report does provide a number of statements which point to its role and objectives.

The SSI annual report states that the SSI has four main functions:

- to provide professional advice to Ministers and Central Government departments on all matters relating to the personal social services;
- to assist local government, voluntary organisations and private agencies in the planning and delivery of effective and efficient social care services; and assessing the performance of local councils with social care responsibilities, including Better Value;
- to run a national programme of inspection, evaluating the quality of services experienced by users and carers;
- to monitor the implementation of Government policy for the personal social services.

The Inspection Division of the SSI is responsible for a programme of national inspections in order to:

- evaluate the quality of social service provision;
- improve the efficiency and effectiveness of social services delivery;
- provide information to influence social care and health policy development and implementation;
- support the Secretary of State's regulatory responsibility for child care provision.

The SSI Inspection Division's work involves finding out through inspections just how effective personal social services are whilst making sure that providers are doing what the law and government policy require, acting in accordance with good professional practice, and meeting the needs of the people who use their services.

The inspection framework

The inspection programme is delivered through the six inspection groups managed by Assistant Chief Inspectors. They are responsible for evaluating the quality of aspects of social

services in all local councils. Some inspections cover broad areas of services, such as children's services or services for older people. Others focus on a more specific theme such as adoption or welfare to work. They also target inspections on councils where a particular service has been identified as causing concern.

The inspection framework includes the following:

- During an inspection, SSI will look closely at all aspects of the quality of a service, as it is received by the people who use it and their carers. An assessment of its quality is formulated using a set of published standards and criteria.
- SSI standards are statements of quality of services expected and are derived from Government policy, legislation and regulation, and professional knowledge about what constitutes good quality services and what contributes to good practice and effective management.⁴⁵
- Criteria (detailed statements explaining exactly what is expected from the service for it to meet the required standards) are then set.
- At the end of the inspection, a report is written and published for the people providing the services and those who use them, describing what the SSI thinks is good about the services, and making recommendations for improvements.
- Follow up checks are made to assess whether changes have been made following recommendations.

The inspection process includes the collection and analysing of information from a wide range of sources. Inspectors make professional judgements based on regulatory requirements and expertise. Inspectors provide information to inform development of Government policy.

The SSI/Audit Commission joint review team brings together expertise from the two bodies to review the performance of all local council's social services responsibilities. Joint reviews consider how well councils meet individual needs, shape services, manage performance and manage resources. Inspection and joint review programs aim to be complementary and are scheduled to build on the work of each other.⁴⁶

The inspection programme is arranged so that each local council with social services responsibilities will have three inspections in the five years between joint reviews. These will consist of a child care services inspection, an adult care services inspection, and a third inspection, which will have a more specific focus on an area of high priority. In addition, inspections of local council inspection units are undertaken, as well as targeted inspections in poorly performing councils.

The SSI Social Care Regions undertake ongoing monitoring of the progress of local councils in implementing the Department of Health's national priorities guidance and specific aspects of the Government's policy agenda, major ministerial initiatives and action plans to address the recommendations of inspections and joint reviews.

The SSI holds annual reviews bringing together information about the performance of each local council from performance assessment framework indicators, inspections and joint

⁴⁵ SSI standards are specified prior to inspections so that social services departments and agencies can understand the basis on which their services are being inspected. They are made available so that they can be used as a tool by local councils to assess their own standards and audit their progress.

⁴⁶ Social Services Inspectorate (2000) *The Social Services Inspectorate: Who we are and what we do*.

reviews and regional monitoring to form an overall assessment. A meeting is then held between the SSI Social Care Region and the council to review their performance.

Internal evaluation of the SSI

There is no evidence to suggest that the SSI evaluates its own performance. The annual report of the SSI focuses almost entirely on the quality of personal social services and the achievement of particular targets by the councils providing social services.

The SSI does state, however, that they continually review and assess their work to identify areas where they need to improve. This is achieved in a number of ways, including:

- benchmarking their performance against other inspectorates;
- reviewing the effectiveness of their work and developing it in light of what they have learnt (these do not, however, appear to be published);
- responding to complaints made to the Assistant Chief Inspector of the relevant inspection group or region;
- reviewing activities as part of the Better Quality Services programme that applies to all central government departments to ensure that they are achieving the best quality and value for money;
- consulting with key national organisations, such as the Association of Directors of Social Services, the British Association of Social Workers and the Social Care Association, and the LGA;
- using questionnaires to seek feedback on the quality of their inspections and regional performance assessment activity to help them review their practice and methods.

External evaluation of the SSI

The Select Committee on Health is responsible for examining the expenditure, policy and administration of the Department of Health and its associated public bodies. While, since 1997, it has heard evidence annually on the expenditure on public health and personal social services, it has undertaken no review of the SSI.

A survey of local authorities on the impact of inspection by the Local Government Association which sought views from social services departments on the SSI as well as joint reviews between the SSI and the Audit Commission found strong support for inspection with inspection being seen as a catalyst for improvement and for enhancing accountability. However, respondents to the survey also found inspection to be resource intensive on authority staff, to be lacking in consistency and to not be proportionate. A significant proportion of respondents agreed that inspection had led to improved services for citizens and users and that inspection had helped the local authority become a learning organisation. However, there was less clear agreement on whether SSI inspections had led to innovation or whether the public understands the purpose or value of inspections.

The survey also evaluated responses to joint SSI and NHS Performance Management reviews of NHS systems. Respondents felt that the SSI inspections provided a catalyst for improvement. Responses tended to point to the style of the SSI inspection, noting that it was not adversarial, but rather challenging and the approach was one which was supportive and positive. The regulatory approach of the SSI may point to the reasons for the positive response of the inspected bodies to the inspection process. The respondents identify a professional dialogue (seen as “collaborative” and a “style of partnership (rather than

policing”) between the SSI and the authorities and attach positive improvements to this. On the other hand, some respondents identified the inspection process as being “undermining” and providing a “disincentive for staff by undermining confidence and commitment”, with a tendency to focus on “process at the expense of outcomes”. The SSI was also viewed to have an impartial and consistent approach in carrying out inspections which is seen as fair and rigorous. One respondent stated “style of inspection does not provide any difficulties, apart from being resource-intensive”. The SSI inspections were also viewed as being evidence based. However, like other inspection regimes, the SSI was identified as being resource intensive on authorities. Respondents stated, for example, that the inspections are “very resource-intensive for the depth needed, and the reviewers are here for eight weeks, but not full time” and “they also place significant demands on staff”.

Audit Commission

The Audit Commission was established in 1982 and became operational in 1983, with statutory responsibilities to regulate the audit of local authorities in England and Wales, and to promote improvements in the economy, efficiency and effectiveness of local government services.⁴⁷ In 1990, its role was extended to include local NHS bodies. In 2000 it was given the additional statutory responsibility for carrying out best value inspections of certain local government services and functions.

The Commission is an executive non-departmental public body which operates independently of Government and is largely self-financing, with income being derived mainly from fees charged to local authorities and NHS bodies for audit work. The Commission is sponsored jointly by the Department of Environment, Transport and the Regions, the Department of Health and the National Assembly for Wales; and is steered by a board of Commissioners who are collectively responsible for all of the Commission’s activities.

The Audit Commission consists of a Controller who leads the permanent staff the Commission who are organised into six Directorates: Inspection, Public Services Research, Audit Policy and Appointments, Corporate Resources, People Development and Performance Development.

The main functions of the Audit Commission are:

- appointing auditors to all local government and NHS bodies in England and Wales;
- setting standards for those auditors through the Code of Audit Practice, and regulating the quality of audits;
- inspecting local authorities’ compliance with their best value responsibilities under the Local Government Act 1999;
- carrying out national studies designed to promote economy, efficiency and effectiveness in the provision of local authority and NHS services;
- defining comparative indicators of local authority performance that are published annually;
- making arrangements for certifying grant claims and returns;
- receiving and, where appropriate, following up on information received from whistleblowers in local government and NHS bodies under the Public Interest Disclosure Act 1998;

⁴⁷ Audit Commission *Introducing the Audit Commission’s audit regime*.

- working with the Commission for Health Improvement in reviewing the work of NHS bodies;
- working jointly with the Social Services Inspectorates in England and Wales and OFSTED, Estyn, OHMCI on inspections and with the Housing Corporation on value-for-money reviews.⁴⁸

The DETR considers the first five of these functions to be the most important.⁴⁹

Role of the Audit Commission

The Audit Commission “aims to be a driving force in the improvement of public services by promoting proper stewardship of public finances and by helping local authorities and the NHS to deliver economic, efficient and effective services.”⁵⁰

Strategic objectives of the Commission for:

- *Audit supply*: to maintain its low-cost, high-quality audit regime, based on a mixed market of private sector and public sector suppliers

The audit framework

The Audit Commission is responsible for appointing auditors and determining their terms of appointment, as well as for preparing the Code of Audit Practice, which prescribes the way in which auditors are to carry out their functions.

The Commission’s model of public audit (Code of Audit Practice) reflects the concept of ‘integrated audit’ in which each element of the audit aims to inform the other elements. The Commission applies a risk-based approach to audit planning, which requires appointed auditors to assess the relevant risks that apply to audited bodies and their corporate governance arrangements. This risk-based approach aims to give auditors flexibility to tailor the nature and conduct of audit work to the circumstances of the audited body by directing their audit effort to areas of greatest risk. There are three elements to the audit, set out in the Code of Practice:⁵¹

- the financial aspects of corporate governance – auditors consider whether the audited body has adequate arrangements to ensure the legality of transactions that might have significant financial consequences, ensure that its financial standing is soundly based, satisfy itself that its systems of internal financial control are both adequate and effective in practice, and maintain proper standards of financial conduct and to prevent and detect fraud and corruption;
- the accounts – auditors are required to audit the financial statements and to give their opinion whether they give a true and fair view of the financial position of the audited body, whether they have been prepared properly, and for specified NHS bodies, on the regularity of the expenditure and income;

⁴⁸ Audit Commission (2000) *Annual report year ended 31 October 1999*.

⁴⁹ Department of the Environment, Transport and the Regions (2000) *Financial management and policy review of the Audit Commission: Stage 2*.

⁵⁰ Audit Commission (2000) *Annual report year ended 31 October 1999*.

⁵¹ Audit Commission *The Audit Commission’s audit regime: Introducing the Audit Commission’s audit regime*.

- aspects of performance management – auditors are required to review and report on the audited body’s arrangement to secure efficiency, economy and effectiveness in its use of resources, including the use of resources in specific services and functions.

Reviews of aspects of performance management may include those arising from the Commission’s national studies, which are designed to promote good management practice and the best use of public money in specific services and functions. Auditor’s work may also cover topics that have been identified locally.

Auditors of specified local government bodies also have a responsibility to review and report on the audited body’s arrangements for preparing and publishing specified performance information, and compliance with statutory requirements for preparing and publishing its best value performance plan (BVPPs).

In conducting the audit the Code of Practice requires the auditors in planning their audit approach to:

- determine where to direct their work and allocate resources according to the circumstances and risks that apply to the audited body;
- view each part of the audit in the context of the whole or integrated audit;
- establish effective co-ordination arrangements with internal audit and co-operate with, and consider the work of, other auditors, inspectors and statutory review agencies where appropriate;
- adopt a constructive and positive approach;
- inform the audited body’s members or officers of the matter of substance or significant issues arising from the auditor’s work;
- establish effective follow-up arrangements to review whether the audited body has properly considered any matters identified during the current or previous audits;
- co-operate with other external auditors and the Commission to facilitate the effective transfer of good practice between audited bodies.

During the year, auditors provide audited bodies with a range of reports, including:

- an opinion on the financial statements, and other opinions required;
- for specified local government bodies, a statutory report on the audit of the best value performance plan;
- where appropriate, a report dealing with matters that the auditor considers to be in the public interest.

Evaluation of the impact of the Audit Commission

The Commission undertakes to measure and monitor a range of indicators of its own performance. The indicators relate to the performance of the Commission, of its appointed auditors, and of District Audit, its arms length agency. Indicators of the Audit Commission’s performance include the number of reports published and copies sold, the rate of fee increases to audited bodies, the central costs as a percentage of gross income (including value for money studies, auditor appointment, auditor support, performance indicators, corporate management and overheads), the percentage of letters replied to within 3 working days, and staff turnover and sickness. Indicators of appointed auditor’s performance include timely delivery of audit opinions, timely delivery of management letters, compliance with Code of

Audit Practice, and value improvements⁵² (this is dependent on the nature of the studies undertaken and in particular whether the areas studied present opportunities for financial savings – the Commission is currently looking at how best to assess and report on changes resulting from research projects).⁵³

The Department of Environment, Transport and the Regions has conducted two reviews of the Audit Commission (*Financial Management and Policy Review of the Audit Commission – Stages 1 and 2 or FMPRs*) to determine whether the Audit Commission is structured in the most effective way in securing productive working relationships both externally with its clients, government departments and other organisations and inspectorates operating in the field, and with the others internally to carry out its functions; to determine whether the Audit Commission has suitable procedures and internal controls in place to ensure value for money and safeguard regularity and propriety; and to determine whether the Audit Commission has suitable procedures in place to exercise appropriate control over appointed auditors and the quality of their work. This review raises a number of issues around measuring the impact of the Audit Commission.

The DETR report states that the “Audit Commission does not directly control the performance of the audited bodies but instead acts to influence their pursuit of efficiency. Effective indicators of performance for influencing bodies are notoriously hard to develop. As part of a process of measuring its performance, the Commission has developed a system of ‘Value for Money Indicators’ (VFMI) which seek to track changes to key performance indicators at audited bodies in relation to areas which been the subject of a national VFM study. In part, this is intended to monitor the impact of the Commission and this has been quite effective. However, VFMI are expensive to collect, and give a partial snapshot view rather than the continual progress, which would be ideal. The Commission has been reluctant to publicise these indicators as a measure of its own performance, since they are good tools to encourage improved performance by audited bodies and to make them explicit performance indicators for the Commission could reduce their effect. Of the fourteen VFMI follow ups the Commission has undertaken to date, eight show favourable change, four show mixed results and two show little or no improvement.”⁵⁴

The DETR also note that the Commission is “keen to improve the measurement of its own performance” and it has undertaken an external review of its own performance indicators and is considering how to amend them. The DETR identifies two activities to measure – encouraging proper stewardship of public funds and promoting improvement in public services. It notes that measuring the Commission’s performance in relation to either of these activities is not straightforward. With regard to stewardship, the DETR gives two examples of the difficulties of measuring the Commission’s contribution: “Firstly, does a high level of detected fraud indicate Audit Commission success, or failure, or neither? Secondly, how does one measure ‘assurance’ to the public?”⁵⁵ With regard to the Commission’s role of promoting improvement in public services, the DETR notes that the Commission faces a constraint in that the Commission and its auditors cannot force audited bodies to improve their

⁵² Value improvements identified in 1998/1999 were £20 million for Local Government and £5 million for the NHS.

⁵³ Audit Commission (2000) *Annual report 1999*.

⁵⁴ Department of Environment, Transport and the Regions (2000) *Financial Management and Policy Review of the Audit Commission: Stage 2*.

⁵⁵ Department of Environment, Transport and the Regions (2000) *Financial Management and Policy Review of the Audit Commission: Stage 2*.

performance, only encourage them to do so. The DETR argue that “where audited bodies are successful, as is only natural they tend to consider themselves to ‘own’ the changes rather than attribute them to auditors or the Commission. Where audited bodies do not change their behaviours, neither the Commission nor auditors can force them.” The DETR argue that despite these difficulties, the Audit Commission should develop a more comprehensive set of performance indicators for its own work and should publish targets for achievement in the main indicators.

In its annual report, the Audit Commission outlines the areas in which it is aiming to develop indicators to measure its own performance. These include performance measures relating to the contribution of the Commission to improving public services, specifically changes resulting from national research and inspections, financial savings resulting from national studies, and timely delivery of inspection programmes. In addition, the Commission are further developing financial and service indicators which focus on fee increases, central costs, efficiency savings and speed of response to mail and telephone calls.⁵⁶

No value for money audits are undertaken of the Audit Commission. While the FMPRs of the DETR do review the performance of the Audit Commission approximately every five years, they do not undertake value for money audits. The DETR states that “the Commission is sometimes seen as being in an anomalous position in that, whilst it examines value for money arrangements for all its audited bodies, it is not itself subject to value for money audit. Although the National Audit Office (NAO) is the auditor for the Audit Commission, unlike the Commission it only reviews value for money at a selection of the organisations it covers. By NAO standards the Audit Commission has low total expenditure and is a low risk. Therefore, to date, the NAO has not carried out value for money audit on the Commission and this seems unlikely to change without a fundamental change in the overall NAO approach.”⁵⁷ The DETR argue that “the absence of an external value for money review gives rise to accusations of the Commission not practising what it preaches”.

The DETR’s FMPR also reviews the changes in central costs of the Audit Commission and the measures of cost control employed by the Commission.

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