Corporate governance

Improvement and trust in local public services
The Audit Commission is an independent body responsible for ensuring that public money is spent economically, efficiently and effectively, to achieve high-quality local and national services for the public. Our work covers local government, housing, health and criminal justice services.

As an independent watchdog, we provide important information on the quality of public services. As a driving force for improvement in those services, we provide practical recommendations and spread best practice. As an independent auditor, we monitor spending to ensure public services are good value for money.

Key Messages

- Corporate governance is critical to providing high-quality public services. Governance weaknesses have led directly to service failure, sometimes with tragic consequences.
- Corporate governance is critical to raising trust and understanding among the public in local public services: by improving the quality of services and by being open and honest about performance and mistakes.
- Corporate governance is not a 'bolt-on'. Well-governed organisations effectively combine both the traditional 'hard' aspects of controls assurance and the 'soft', cultural characteristics of effective leadership and openness to promote effective decision making and clear accountability in a complex and ambiguous environment.
- Well-governed organisations reflect diverse views in their decision making, producing greater ownership among stakeholders and injecting clarity of purpose.
- For public sector regulation to be effective, it must stretch to encompass the governance framework within which services are provided. Greater collaboration between regulators, auditors and inspectorates, through Strategic Regulation will provide the capacity and governance needed to grant organisations greater freedoms and flexibilities.

1 Corporate governance affects the quality of services. Major weaknesses in governance arrangements have contributed to service and organisational failure, often with serious and sometimes with tragic consequences. Consistently high-performing organisations, on the other hand, display effective governance arrangements. Both examples show that corporate governance is not a 'bolt-on' option for organisations, but fundamental to how it delivers services.

2 In this way, corporate governance has a critical impact on the level of trust that the public is willing to place in public bodies and services. Our research shows that the public's trust is affected in two ways: by the quality of services that they and their family and friends experience; but also by the willingness of organisations to be open and honest about their performance (including mistakes) and to do something to remedy poor performance. Positive performance in these two areas are the outcomes of effective corporate governance.

3 There are different definitions and interpretations of corporate governance. The Audit Commission defines corporate governance as:

   The framework of accountability to users, stakeholders and the wider community, within which organisations lead and conduct their functions, and take decisions to achieve their objectives.
Well-governed organisations are able to balance a number of competing and sometimes conflicting targets and tensions. They are therefore able to reconcile multiple accountabilities. They do this by effective interaction of 'hard' characteristics, usually described as systems and processes, and 'soft' characteristics, such as the organisation's culture. Those that appear to be most influential are:

- **effective leadership** that generates clarity of understanding about strategy, objectives, and values, and about who is responsible for contributing to achieving those objectives;
- reliable information produced by **robust and effective systems and processes** – the "building blocks" of good governance – enabling the right decisions to be reached about what needs to be done in order to achieve objectives;
- a culture based on **openness and integrity** in which decisions can be challenged and accountability is clear; and
- an **outwardly focused perspective**, with clear communication and dialogue between decision makers and service users and the public.

It is not easy for organisations to understand how well these features interact. They do come together at the point at which decisions are made. Transparent, high-quality **decision making**, including the known basis on which information is accepted or disregarded, coupled with effective scrutiny and challenge is the output of good governance.

Ultimately, good governance and effective decision making depends on the quality of relationships among those in governance positions. Executives and non-executives work in partnership, but this requires relationships to be based on trust and mutual recognition of the boundary between their roles. The non-executive function must be sufficiently confident and competent to be able to hold the executive to account. The executive must establish the framework of structures, systems and processes within which that accountability can be rendered. The relationship between the chief executive and the chair or leader will set the tone for the rest of the governing body and throughout the organisation.

The characteristics of good corporate governance are common to all public organisations, regardless of sector, but making them a reality and sustaining them is difficult. Performance varies in each part of the public sector. Many organisations struggle to set a clear direction and to involve users and the public in decision making. They also have problems with the quality of information used for decision making and with valuing and enabling the non-executive role. Non-executives are not being used to their full effect in police, health and probation. There are similar concerns for local non-executive councillors in fulfilling their role of scrutiny.
Auditors' views of corporate governance across the public sector are that:

- Performance management is an area of weakness in the public sector. In local government, for example, approaching three in four (72 per cent) councils are working to improve performance management following their comprehensive performance assessments (CPA). Around one-half of police forces inspected by Her Majesty's Inspectorate of Constabulary (HMIC) since 2001/02 had performance management weaknesses.

- Most organisations in the public sector are in reasonable financial health, but this is seen as the area of highest risk in the NHS, as health bodies work to meet the targets of the NHS Plan.

- Risk management and internal controls are weakest in local government, police authorities and probation boards.

The quality of information feeding the decision-making process needs to improve in every sector, but particularly in the NHS and the police.

In the police, there is a need to clarify the roles and relationships between chief constables and Police Authorities. In probation, there is a need to clarify the proper role of the local board within a tightly defined national policy and framework.

Local government continues to experience problems in making scrutiny work effectively, although signs of progress are now evident.

All public sector organisations need to work to improve the public's trust in their competence and honesty. Improving trust in local public bodies is also a challenge for regulators, auditors and inspectors.

Strategic Regulation

The Audit Commission will continue to promote Strategic Regulation. Centralist command and control supported by a plethora of targets is counterproductive and the general trend in public service is to reward high-performing local organisations with greater freedom in budgetary control and service planning. But before such freedoms can be granted — particularly for new organisations, like foundation hospitals and children's trusts — confidence is needed in their ability to lead and manage their organisations to deliver high-quality and cost-effective services. This confidence is obtained only through greater collaboration between inspectors — they must share the information that leads to overall judgements about corporate and service performance and capacity. CPA in local government is a good example of this.