High pressure system
# Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Introduction</td>
<td>1</td>
</tr>
<tr>
<td>Highlights</td>
<td>2</td>
</tr>
<tr>
<td>Governance framework and the AGS</td>
<td>4</td>
</tr>
<tr>
<td>- Annual best practice review</td>
<td></td>
</tr>
<tr>
<td>- A window for stakeholders</td>
<td></td>
</tr>
<tr>
<td>- How helpful is the AGS?</td>
<td></td>
</tr>
<tr>
<td>Risk management</td>
<td>10</td>
</tr>
<tr>
<td>The audit committee</td>
<td>13</td>
</tr>
<tr>
<td>Scrutiny</td>
<td>16</td>
</tr>
<tr>
<td>Partnership working</td>
<td>20</td>
</tr>
<tr>
<td>Fraud, corruption and the Bribery Act</td>
<td>23</td>
</tr>
<tr>
<td>The explanatory foreword</td>
<td>27</td>
</tr>
<tr>
<td>Public accountability</td>
<td>34</td>
</tr>
<tr>
<td>- Annual reporting</td>
<td></td>
</tr>
<tr>
<td>- Managing complaints and information requests</td>
<td></td>
</tr>
<tr>
<td>People</td>
<td>37</td>
</tr>
<tr>
<td>- Capacity and capability</td>
<td></td>
</tr>
<tr>
<td>- Standards</td>
<td></td>
</tr>
<tr>
<td>- Gender diversity</td>
<td></td>
</tr>
<tr>
<td>Appendix A: Roundtable attendees</td>
<td>40</td>
</tr>
<tr>
<td>Appendix B: NHS report highlights</td>
<td>41</td>
</tr>
<tr>
<td>Appendix C: FTSE 350 report highlights</td>
<td>43</td>
</tr>
</tbody>
</table>
Introduction

Welcome to Grant Thornton’s first Local Government Governance Review. It comes at a challenging time, as councils face intense pressure to deliver unprecedented funding cuts, organisational change and innovation in service delivery, while meeting public demands for greater transparency in decision-making and performance.

Effective governance is essential if senior officers and members are to meet these exacting challenges. Ironically though, those processes that ensure good governance are at risk from the conflicting demands for reduced spending and a re-prioritisation of resources.

Against this background, our review evaluates the soundness of existing systems for operating in this high-pressure environment. We analysed the survey responses of more than 100 senior council officers and members, we carried out desktop reviews of the most recent governance information published by councils in England, Wales and Scotland, and we hosted a roundtable discussion of key senior stakeholders. We also drew on findings from our recent reviews of governance in the NHS and FTSE 350.

Our aims have been to sound warning alarms where we believe governance arrangements are failing to cope, to suggest areas in need of improvement and, perhaps most importantly, to provide realistic and practical guidance on how local council governance can be made stronger and more effective in UK local government’s high pressure system. In short, to establish a direction of travel towards “the standards of the best”.

Paul Hughes
Director
Public Sector Governance Lead

“We would like to thank everyone who contributed to this review including survey respondents, roundtable attendees and all who carried out the research, analysis and report production.”

Methodology

Our review is based on:

• a desktop review of 200 councils’ 2010/11 AGS and explanatory forewords, comparing them to our best practice criteria
• responses from 120 council senior officers and members to our survey on governance reporting in the AGS and explanatory foreword, and the supporting governance processes
• a roundtable discussion with senior sector figures, public sector governance experts and Grant Thornton sector experts (attendees listed in Appendix A).

Scope

The review covers councils in England, Scotland and Wales. In most cases, findings are presented in aggregate, as differences in results were generally minor. Although only English upper tier councils were reviewed, the findings are equally relevant to English district councils that are subject to the same governance and accountability requirements.

“All authorities should aim to meet the standards of the best and governance arrangements should not only be sound but also be seen to be sound. Governance is about how local government bodies ensure that they are doing the right things, in the right way, for the right people, in a timely, inclusive, open, honest and accountable manner.”

Delivering Good Governance in Local Government Framework, CIPFA/SOLACE, 2007
Highlights

On people

Councillors should rethink their investment in people to ensure good governance.

One fifth of survey respondents said they do not believe their councils have robust enough systems to develop the capacity and capability of officers and members.

Councillors are feeling the pressure in people development, but we believe they need to continue to develop those responsible for governance, honestly self-assessing current training and development effectiveness and investing where necessary.

Our survey showed women occupy nearly 30% of cabinet positions. This compares favourably with the private sector where only 10% of FTSE 350 company directors are female. However, in the NHS, 35% of board directors are women.

There is significant scope to improve gender diversity at the highest level in councils. In particular, we believe councils should consider what more they can do to increase the representation of women as council leaders from the current level of 12%.

Our research found that around 80% of councils carry out annual governance reviews. Experience and anecdotal evidence suggest these reviews are more compliance driven than seeking to emulate best practice.

We recommend councils do more to ensure their practice, especially the beliefs and attitudes of their leadership team, reinforces their ambitions for a stronger governance culture.

On risks

Councillors have strengthened their processes around governance, but more focus is needed on improving their effectiveness and on emerging risks.

Respondents indicated high confidence in their council’s risk management arrangements, with 98% agreeing they were effective at identifying key strategic risks and 96% believing they were effectively managed. However, our research showed governance to be under pressure from funding constraints – all at a time when risks in the operating environment have never been higher.

We believe councils need to work even harder to make their risk management arrangements lean and dynamic. This is likely to mean rethinking their idea of tolerable risk, adopting an ‘opportunity risk management’ approach and making a significant culture shift.

Respondents rated scrutiny as the top priority for improving council governance. More than a third said their council’s scrutiny function was not effective in responding to changing risks and could not demonstrate its value.

Councils need to ensure that their scrutiny functions are effective in holding senior officers to account and improving policy making. But investment will be required, particularly in the training and development of scrutiny committee members.

Audit committees were considered one of the top three strengths of governance by respondents. There was a strong view that audit committees are responding effectively to changing risks and adding value.

We identified excellent examples of audit committees fostering the improvement of risk management and control processes. There is, however, a wide variation in practice and considerable benefits to be obtained by sharing best practice techniques.
The need to deliver innovative services for less increasingly requires councils to work with public and private sector partners. Respondents were, on the whole, positive about partnership working, with 89% saying they were clear about the respective roles – a crucial prerequisite for successful outcomes.

We found that respondents’ positive response to partnership working is at odds with other published evidence. We believe councils may be underestimating the governance challenge that working together presents and recommend they continue to develop their approach to partnership.

More than 90% of respondents said their council was aware of, and had responded to, the heightened risk of fraud and corruption in today’s depressed economy. Some £185 million of fraud was detected in local government last year, but with undetected fraud estimated at 10 times this figure, this area warrants close attention.

The risk that fraud will go undetected – and the knock-on effect on public confidence – means councils must remain vigilant and continue to strengthen their anti-fraud and corruption arrangements.

On reporting

Councils can significantly improve stakeholder engagement in their reporting.

Over a third of respondents say they do not find their council’s annual accounts helpful in explaining its financial position. In contrast, the vast majority of respondents (95%) believe their council’s explanatory foreword to the accounts provides a clear and concise introduction. Whilst generally compliant we noted that forewords varied greatly in content and approach.

We recognise that the inherent complexity of council accounts limits their usefulness to non-expert readers. In this context, we believe that undertaking a user review and best practice assessment of the explanatory foreword could improve its quality and usability as an introduction to the accounts, as well as boosting council transparency and accountability.

Three-quarters of councils publish their Annual Governance Statement (AGS), the primary indicator of compliance with the governance code, in the annual accounts on their website. Of the remainder, some publish statements elsewhere on their websites, although quite often in hard-to-find locations. Some councils did not make them available online at all.

We believe all councils should publish their AGS, with their annual accounts, on their website where it can be easily found.

98% of respondents agreed their AGS was clear and understandable. While most do comply, when compared to best practice we believe there is room for inclusion of many features that would enhance interest and value.

We suggest that better planning, tracking and evaluation could bridge the apparent disconnect between the perceived and actual merits of the AGS.

On a new way forward

We believe there is a strong case for all councils to publish a consolidated annual report.

So few councils produce consolidated annual reports incorporating summarised financial information, the AGS and key performance information, that we were not able to undertake a useful review across the sector.

Annual reports can engage the public and other stakeholders by providing the information to enhance accountability and transparency in, for example:

- stewardship of scarce resources
- governance effectiveness
- operational performance.

Councils have a responsibility to local taxpayers and other stakeholders to report information in a consistent, understandable and engaging way. We believe a well-executed consolidated annual report, drawing from best practice in other sectors, would provide the solution.
Annual best practice review

Councillors are responsible for ensuring public money is safeguarded, properly accounted for and used to deliver maximum value for their communities. Consequently, their business must be conducted in line with the law and proper standards. It is reassuring, then, that of our survey respondents 80% said they ‘strongly agree’ and 18% ‘tend to agree’ that their councils undertook at least the minimum requirement of an annual review of governance arrangements to ensure compliance with best practice.

Our experience tells us that the majority of councils documented and annually updated local governance codes based around the six core principles set out in the CIPFA/SOLACE Framework – which, from 2007/08, required councils to develop a local code of corporate governance to ensure proper systems are in place to meet their responsibilities.

However, we are also aware that annual reviews often do not consider sector best practice – an absence recognised by many of our local government clients and roundtable attendees. Our concern, therefore, is that the annual review is sometimes completed as a compliance exercise rather than in the spirit of actually doing the right thing, and that there could be far greater efforts to achieve best practice.

The six core principles of governance

1 Focus on the purpose of your authority and on outcomes for the community, as well as on creating and implementing a vision for your local area.
2 Members and officers should work together to achieve a common purpose with clearly defined functions and roles.
3 Promote your authority’s values and demonstrate the values of good governance by upholding high standards of conduct and behaviour.
4 Take informed and transparent decisions and subject them to effective scrutiny and risk management consideration.
5 Develop the capacity and capability of members and officers to be effective.
6 Engage with local people and other stakeholders to ensure robust public accountability.

Delivering Good Governance in Local Government Framework, CIPFA/SOLACE, 2007

We undertake at least annual reviews of our governance arrangements to ensure that we comply with best practice.

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<tr>
<th>Response</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Strongly agree</td>
<td>80%</td>
</tr>
<tr>
<td>Tend to agree</td>
<td>18%</td>
</tr>
<tr>
<td>Tend to disagree</td>
<td>2%</td>
</tr>
<tr>
<td>Strongly disagree</td>
<td>0%</td>
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</table>
A window for stakeholders

The AGS gives councils a mechanism to demonstrate their positive governance culture and achievements. We believe many could do more to realise this opportunity.

Councillors must produce an AGS to report publicly on how they have complied with their governance code and describe any governance issues, including how they will be addressed. This is a requirement under the CIPFA/SOLACE framework and, in the absence of an annual report, makes the AGS a key window through which councils display their governance credentials.

Our assessment of both the availability and prominence of the 2010/11 AGS for more than 200 UK councils suggests that many have some way to go to make their draft or final AGS accessible to the public.

Although no longer formally required to do so, 80% of councils posted a draft AGS on their website. However, the remainder did not provide them even when we requested them and explained the purpose of our request. A number of councils suggested we use Freedom of Information (FoI) Act provisions.

In October 2011, we visited 150 council websites to find the audited accounts and review the final version of the AGS. Of these, 75% included the AGS within the statement of accounts, with 38% of these having the AGS prominently displayed and 20% providing evidence that the AGS had been re-signed at the audit opinion date by the leader and chief executive.

While final re-signed AGS may have been located elsewhere on council websites, we were unable to find them.

This is surprising, at a time when the public is demanding greater transparency and openness from its public services. (See page 34 for further aspects of public accountability.) If a council does not use the AGS to showcase their focus on good governance, it may be reasonable for stakeholders to conclude that this reflects its underlying governance culture.

We believe that many councils could be doing more to demonstrate that their AGS has been properly approved and to make it more accessible.
Nearly all (98%) of our survey respondents said their AGS gave a clear picture to stakeholders of their governance arrangements and any significant weaknesses. This is a very positive response, with almost two thirds of those surveyed ‘strongly agreeing’ with the statement. However, it was noticeable that chief executives were more reserved in their assessment. They were likely to ‘tend to agree’ and were the only respondents that ‘tended to disagree’.

Meanwhile, our desktop review of best practice showed councils’ AGS on average scored 2.3 out of 5. This means that, while they are compliant, they only just balance comprehensiveness of content with a concise and clear message. Some key highlights from the sub-categories are shown on page 7.
**Methodology and findings**

We reviewed the AGS against our best practice criteria based on the CIPFA/SOLACE framework and guidance notes. Two additional questions considered essential for an effective AGS were included:

1. How well does the AGS describe what level of assurance is required from the governance framework for the year in question?
2. How well does the AGS conclude on the level of assurance provided by the governance framework for the year in question, including whether this is sufficient?

We scored the AGS against 11 questions using a five-point scale:

1. Missing
2. Part missing
3. Minimum
4. Enhanced
5. Standard-setting

The average for all of the questions was 2.3.

Specific question outliers (+/− 0.5 of average score) are shown in the chart.

There were higher than average scores for the comprehensive inclusion of ‘the acknowledgement of responsibility for ensuring there is a sound system of governance’ and the description of ‘the purpose of the governance framework’. This, though, reflected the largely boilerplate nature of the early sections of the AGS which have less scope for local tailoring.

The results for the two questions around sufficiency of assurance scored poorly, as did those describing what had been done (and what is yet to be done) to resolve significant control issues from the previous year.

These results reveal a big perception gap between the perceived and actual usefulness of the AGS to stakeholders (shown by the difference between the positive views of our survey respondents and our quality score). They suggest that councils have some way to go to achieve best practice.

We believe councils can make their AGS much more useful by showing they have determined what assurances they need from governance arrangements and concluding explicitly where they have received sufficient assurance.

We also think that councils need to provide a clearer picture to stakeholders, year-on-year, of how significant issues have been dealt with and what assurances demonstrate this.
The AGS remains an opportunity waiting to be realised

This year’s research and our experience since 2007/08 of reviewing AGS, and the processes used to produce them, indicates that these important documents are often not given the attention they deserve. In many cases, the focus is line-by-line compliance with the framework and guidance notes. The opportunity to ensure the AGS fulfils its intended purpose – namely, clearly documenting how council governance arrangements provide sufficient assurance to achieving their vision and strategic objectives – is yet to be fully grasped.

We found the AGS rarely addresses fundamental questions such as:
• what is the level of assurance we are trying to achieve this year?
• will the processes and controls we are describing provide sufficient assurance?
• what assurances have these processes actually given and to whom?
• have we achieved the level of assurance we need and, if not, what are we going to do about it?

Statements are usually:
• written and presented by internal audit – a potential conflict issue given their formal role in reviewing the AGS
• reviewed by senior officers and members for minor details rather than with a strategic focus.

We found that statements are generally:
• prepared at year end rather than all year round
• amended incrementally each year
• not updated to reflect significant issues arising between the production of the draft accounts and the audit opinion date.

Statements are:
• unclear about whether issues recorded are significant in achieving the council’s vision
• unclear as to which part of the framework identified the issue and what this means for the wider governance processes
• often vague in articulating ‘significant’ issues identified that year and in following up action on the previous year’s issues
• rarely SMART in action planning.

Governance framework and the AGS

Missing the big picture

Inadequate ownership and challenge

Significant governance issues poorly articulated

Static, year end focus
What should councils do?

To add real value we believe the AGS should:
- have greater status within the council’s management and reporting processes as the key document that records the planned and obtained assurances around the achievement of the vision and strategic objectives
- be owned from the top and used to plan and monitor internal and external assurance gathering throughout the year
- be fundamentally reviewed each year so that it highlights what is significant and excludes what is not
- have only significant weaknesses recorded with SMART action planning
- provide a robust, transparent and honest assessment of the year’s governance framework.

Significant governance issues identified in 2010/11

The average AGS we reviewed was 11.3 pages long and included 4.5 significant governance issues. Based on our analysis of survey responses, the most common significant issues identified for 2010/11 are shown in the chart below. These include internal control, relationships and procurement in England, Scotland and Wales. In England, there is a particular focus on savings programmes, transformational issues, data quality and IT security. In Scotland and Wales, capability is one of the most common responses.

<table>
<thead>
<tr>
<th>Country</th>
<th>Internal control issues</th>
<th>Risk management issues</th>
<th>Relationships/procurement</th>
<th>Capability issues</th>
</tr>
</thead>
<tbody>
<tr>
<td>Scotland</td>
<td>13</td>
<td>9</td>
<td>8</td>
<td>7</td>
</tr>
<tr>
<td>Wales</td>
<td>13</td>
<td>6</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>England</td>
<td>46</td>
<td>42</td>
<td>36</td>
<td>33</td>
</tr>
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</table>

<table>
<thead>
<tr>
<th>England</th>
<th>Savings programmes/ transformation issues</th>
<th>Internal control issues</th>
<th>Data issues/IT security</th>
<th>Relationships/procurement</th>
</tr>
</thead>
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Risk management

High levels of confidence in the capacity of council governance processes to identify and manage significant risks pay testimony to years of effort. But we believe that, with funding constraints, councils must now be more creative. Risk aversion is no longer an option.

A decade ago, council risk management was often led by an insurance or health and safety officer with little corporate profile. Today, it is on the cabinet and audit committee agenda and is supported by dedicated risk management specialists. This increase in importance of risk management was reflected in our survey results that suggest a high level of confidence in the capacity of governance processes to identify and manage significant risks.

The vast majority of survey respondents (98%) agreed that their council’s governance arrangements were effective at identifying key strategic risks, with almost half ‘strongly agreeing’ with the statement. Chief executives and directors of governance were more likely to ‘strongly agree’, with directors of finance, audit committee chairs and heads of internal audit ‘tending to agree’.

Almost as many (96%) felt that these arrangements led to the effective management of risks, again with around half ‘strongly agreeing’. Heads of internal audit were more likely to ‘tend to agree’.

Slightly fewer (90%) respondents agreed that risk management was embedded into the culture of the council. More said they ‘tend to agree’ than ‘strongly agree’ and 10% said they ‘tend to disagree’. Responses were very similar, irrespective of position.

<table>
<thead>
<tr>
<th>Our governance arrangements are effective in identifying risks to the achievement of the council’s key objectives.</th>
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<tbody>
<tr>
<td>Strongly agree</td>
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<tr>
<td>Tend to agree</td>
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<tr>
<td>Tend to disagree</td>
</tr>
<tr>
<td>Strongly disagree</td>
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<table>
<thead>
<tr>
<th>Our governance arrangements are effective in ensuring that key risks are appropriately managed.</th>
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<tr>
<td>Strongly agree</td>
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<tr>
<td>Tend to agree</td>
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<tr>
<td>Tend to disagree</td>
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<tr>
<td>Strongly disagree</td>
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<table>
<thead>
<tr>
<th>Risk management is embedded into the culture of the council, with those responsible recognising it as an integral part of their job.</th>
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<tr>
<td>Strongly agree</td>
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<td>Tend to agree</td>
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<tr>
<td>Tend to disagree</td>
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<tr>
<td>Strongly disagree</td>
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Responding to change
Respondents rated ‘improved risk management’ as the top outcome from their governance frameworks. Improving scores over the years in the independent external use of resources assessment is further evidence of this trend.

UK local government is made up of a large number of complex, multi-functional organisations, raising and spending billions of pounds and serving tens of millions of people. Council investment in robust risk management processes has, no doubt, supported success in delivering capital projects on time and within budget expectations, maintaining continuity of service in crises, protecting vulnerable people and supporting communities.

On the whole, we believe local government manages risk well. However, strategic risks identified by our survey respondents indicate increasing pressure on current arrangements (see opposite). Specifically, those risks around lower funding, reduced capacity and increasing demand.

Funding pressures mean that councils may no longer be able to maintain internal risk management resource levels – just as they are facing increasing levels of risk due to factors such as service transformation, outsourcing and localism.

We believe councils need to rethink their approach to risk management, making some tough decisions about what is tolerable risk. The outcomes of these considerations will need to be fully understood and accepted by officers and members as they will affect how potential service failure is dealt with and managed in the public arena.
Risk management

Opportunity risk management

The Institute of Risk Management (IRM) carried out a review of opportunity risk management approaches in 2009. It concluded that:

- attention to opportunity risk ensures critical new ideas and challenges are properly considered and raises the focus from day-to-day operational issues
- a move to opportunity risk helps broaden the perception of risk and supports a more dynamic, entrepreneurial business culture
- a change in approach challenges existing mind-sets and improves decision-making, while aligning the risk management and business planning processes.

Making it happen

The IRM suggests delivering an opportunity risk management approach by using stakeholder workshops integrated into existing processes. It recommends keeping it simple, strategic and interactive, perhaps by using traditional SWOT analysis.

Stretched resources

Councils will need to become more creative with the deployment of an increasingly stretched risk management resource. They must learn to:

- control, but not over-control, the most significant risks
- respond to issues rapidly, but proportionately
- enhance their risk management processes to maximise opportunity rather than – as traditionally – minimise risk.

The scale of the service and financial challenge facing the sector means that councils cannot afford to be risk averse. Incremental change is an option available to far fewer councils. Bold decisions will be required and, if these are to be successful, they will need to be underpinned by effective opportunity risk management (see box).

Now that councils are more familiar with concepts of risk, there is scope to move towards a leaner and more dynamic approach, integrated into strategic management. This will require a culture shift for many councils as well as frank discussion with auditors, regulators, central government and strategic partners.
Attention to membership, planning and focus is essential for delivering audit committee value as council agendas evolve. With more than 90% of those surveyed saying their committee is already effective, we encourage councils to build further on this success.

Although not mandated, over the past few years, most councils have chosen to have audit committees. These have largely developed a useful and welcome internal challenge function.

Excellent examples of audit committee effectiveness includes ensuring the implementation of audit recommendations and responding to adverse events, such as the Icelandic investments episode. In some cases, cross-party members have worked together to challenge management to deal with governance issues.

The positive development of council audit committees is reflected in our survey, in which 94% of respondents agreed, with 60% 'strongly agreeing', that their audit committee function effectively responded to changing risks and annually demonstrated its value. The responses were consistent across all positions. Audit committees and the audit function were also rated as two of the top three strengths of council governance arrangements.

However, based on our experience, council audit committees vary in effectiveness and more could be done to embed good practice principles. The experience of the corporate sector in undertaking robust annual reviews and providing annual reports to the board on their work are two areas to consider. Other areas are set out in the adjacent chart.

We have an audit committee function that is effectively responding to the changing risks facing the council and can annually demonstrate the value it adds.

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<th>60%</th>
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<td>Strongly agree</td>
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<td>Tend to agree</td>
<td>34%</td>
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<tr>
<td>Tend to disagree</td>
<td>6%</td>
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<tr>
<td>Strongly disagree</td>
<td>0%</td>
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Audit committees – overcoming the challenges

- **Agenda management** – try not to do too much in a meeting as this can lead to rushed consideration of items of business.
- **Boundaries** – gaps or duplication can result from unclear boundaries with management/executive/scrutiny. Keep boundaries clear.
- **Party politics** – use committee time productively and ensure time and valuable points of member challenge are not lost in the noise of council.
- **Focus** – too much precious committee time can be spent on minor or out-of-scope matters rather than on key risks.
- **Self-assessment** – be honest and always ask: Are we doing what we planned to? Do reports give us what we need? What do we need to do differently?
The unprecedented climate facing local government is making the audit committee agenda ever more challenging. This increases the risk of things going wrong, such as applying superficial scrutiny by trying to cover too much ground, or failing to spot new risks resulting from transformation.

So how should audit committees manage the risks to effective operation? We believe the right membership is key. The appointment of a skilled chair with the ability to keep the work of the committee on track is very important. Finance skills can and should be provided by other members. It is also critical that, as a group, members have the right blend of skills, expertise, independence of mind and political neutrality to enable the committee to fulfil its role.

If these criteria are met, then an audit committee may not necessarily need to have independently appointed members to be effective.

Planning and managing the work of the committee throughout the year is also vital to success. Improvements can be made if, at the start of the year, the committee sets out how it will use its limited time most effectively. It should be clear about what assurances are needed around key risks and schedule how, and from what source, it wants to receive them. Maintaining an on-going focus on the content of the AGS is one way of achieving this. Also, clarity about what constitutes ‘reasonable assurance’ will help the committee know when this has been achieved.

Other levers for effectiveness can include member briefings, shorter reports, active collaboration with scrutiny to maximise collective impact, and preparation of an annual chair’s report on the work and impact of the committee.

Independent external challenge, based on observation, interviews and documentation review, is a good way to identify areas where change is needed and help with implementation. Overall, audit committees should constantly raise the challenge: “Are we achieving our objectives most effectively and adding value to the governance of the council?”

Top three key strengths of council governance arrangements identified in our survey:
Tips for audit committee effectiveness

Establishing or reviewing the committee

- Have appropriate, tailored, up-to-date terms of reference reviewed alongside scrutiny.
- Have a good chair supported by audit and financial expertise (including independently appointed members, as required).
- Consider a ‘board secretary’ role to provide effective officer support.

Planning for the year

- Focus on the end point of assurance for AGS.
- Allow members to own the agenda and ensure that this reflects key risks facing the council.
- Ensure the work plan and meeting schedule flow from assurance planning, as well as required training and briefings.

During the year

- Arrange pre-meetings (including with auditors) to organise and prioritise agendas.
- Keep a constant focus on assurance gathering for the AGS and speak up or call officers in if assurances are lacking.
- Challenge vigorously anything that threatens to soak up committee time that is not key to assurance gathering.
- Maintain an awareness of the risk of drift into scrutiny/executive/management roles and gain assurance that matters are being covered in the appropriate place.
- Be willing to flex the work plan, hold an additional meeting or set up a sub-group to deal with important emerging issues and risks.

Year end

- Challenge the effectiveness of the AGS.
- Ensure explanations of the accounts are clear and satisfactory.
- Prepare a report on the effectiveness of the committee during the year (periodically through external review).
- Feed improvements into next year’s plan.
Our survey respondents rated scrutiny as their top priority for improving governance. There is no one-size-fits-all formula for effective scrutiny but we believe that leaders’ attitude towards accountability and challenge is key.

The local government scrutiny function was established in England and Wales more than a decade ago, to hold the executive to account for its decisions and to contribute to evidence-based policy making.

Delivering audit committee effectiveness is a complex challenge. Each council has only one audit committee, with terms of reference restricted to governance, risk, control and audit. Given that councils have a number of scrutiny committees, covering a wide range of issues arising from the work of the council and its partners, ensuring scrutiny has a demonstrable impact on local people is not easy. This is reflected in our survey results.

Two-thirds of respondents said they thought that scrutiny was effective. Directors of governance were more likely to ‘strongly agree’ that scrutiny was effective, while chief executives’ responses were split evenly between ‘tend to agree’ and ‘tend to disagree’.

However, this is much less positive than for many other areas surveyed. In addition, almost 33% of respondents said they believed their council’s scrutiny function was not effectively responding to changing risks and annually failed to demonstrate the value it added.

Respondents rated ‘scrutiny’ as their top priority for improving governance in the council. This was followed by ‘member input and understanding’ and ‘clarity of information and communication’ – both key building blocks in effective scrutiny.

Our roundtable attendees felt the quality of scrutiny varied enormously. A key point of agreement was that the fundamental driver for successful scrutiny is the attitude the leadership takes towards accountability and inviting challenge.

Consultation and inviting challenge is seen as essential for leaders in business as it improves the quality of decisions. We believe local government should be no different and that scrutiny serves as a key part of that challenge process with its ability to bring in the perspective of the service user. Councils need to support scrutiny to discharge this role as effectively as possible. And yet, research from the Centre for Public Scrutiny showed that council spend on scrutiny fell by 20% last year.

We have a scrutiny function that is effectively responding to the changing risks facing the council and can annually demonstrate the value it adds.

<table>
<thead>
<tr>
<th>Response</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strongly agree</td>
<td>18%</td>
</tr>
<tr>
<td>Tend to agree</td>
<td>49%</td>
</tr>
<tr>
<td>Tend to disagree</td>
<td>28%</td>
</tr>
<tr>
<td>Strongly disagree</td>
<td>5%</td>
</tr>
</tbody>
</table>
Top three things that would improve governance, identified in our survey:

- Clarity of information and communication
- Member input and understanding
- Scrutiny
Audit and scrutiny chairs workshop

How effective scrutiny can make a difference.

In spring 2011, with Shared Intelligence, we hosted a workshop for local government audit and scrutiny committee chairs to discuss how their committees could make a difference.

One of the key areas for discussion was major organisational change. We have set out the main points explored below:

Managing change in relation to complex public services can be very difficult.

Scrutiny can help councils by:
• putting a spotlight on the change processes in the most critical local services
• interrogating needs assessments to ensure the approach reflects the current context and future needs
• exploring how options were formulated and who was involved
• holding public sessions that allow interested parties to give evidence.

The risks councils face can be heightened as a result of policy and performance teams being swamped and management information being seen as a second priority. Scrutiny can address these risks by:
• making sure management information is not neglected or allowed to go unchallenged
• ensuring major decisions take into account what the latest management information is saying
• asking how performance and improvement will be managed in the face of significant budget cuts.

Scrutiny can challenge decision-making robustly.

Pre-decision scrutiny, for example, can probe what evidence there is to suggest that a proposed change will achieve the claimed outcomes. It can add real value to crucial decisions before they are taken. If scrutiny is to play this role effectively, questioning and chairing skills will be at a premium.

In relation to both audit and scrutiny there was a real desire among workshop participants to:
• see cuts are based on analysis and assessment of options rather than ‘salami slicing’
• hold officers to account and not allow them to obscure decisions within lengthy papers
• avoid closed decision-making by using audit and scrutiny to arbitrate publicly on the most contentious issues.

KEY WORKSHOP THEMES

“Demonstrate impact from your work.”

“Take the stakeholder perspective.”

“Focus on what really matters.”
Many principles for ensuring effective scrutiny are the same as for the audit committee. For example:

- **Establishing the committee** – get the terms of reference right and appoint a skilled chair and good quality members
- **Planning** – ensure members own the agenda and have SMART objectives for the year
- **During the year** – keep things on track, challenge robustly and respond to necessary changes in plan
- **Year end** – evaluate and report on effectiveness and feed lessons into next year.

Other specific levers for success include incorporating an element of proactive, pre-decision scrutiny into the work plan and incorporating the views of service users. However, there is no magic formula for effective scrutiny and councils organise their scrutiny functions in many different ways.

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**Four principles of effective scrutiny**

1. Providing ‘critical friend’ challenge
2. Enabling the voice of the public and service users to be heard
3. Owned and led by ‘independent-minded’ lay members
4. Improving public services

*Centre for Public Scrutiny, Good Scrutiny Guide, 2006*
**Partnership working**

Delivering services with other public and private sector bodies is now business as usual for many councils. To achieve the best outcomes, we believe local authorities should put partnership governance high on the agenda.

The phrase ‘partnership working’ in the public sector has many applications. It can refer to shared management teams, shared services, strategic partnering, joint ventures and other incorporated delivery vehicles, unincorporated partnerships, commissioning, outsourcing, co-design, co-production and even straightforward contracting arrangements.

Government policies on the Big Society and Open Public Services agendas, alongside the deficit reduction programme, are increasing the need for councils to consider alternative models for service delivery with other public sector bodies, the private sector and third sector entities, including possible ‘spin offs’ from their own organisation.

Shared service arrangements for back office services such as IT, internal audit, revenues and benefits, and payroll have had mixed success in the past, but are now firmly back on the agenda. This includes public-to-public shared services and outsourcing support service provision to private sector partners.

There are some high-profile examples of the planned merger of frontline service delivery, such as the Tri-Borough partnership of Hammersmith and Fulham, Westminster, and Kensington and Chelsea, and even full-scale ‘constitutional’ mergers or wholesale outsourcing of services.

When done well, partnership working boosts capacity and improves performance, value for money and the quality of services. The Audit Commission’s use of resources good practice database and the Local Government Improvement and Development website include examples of successful partnerships, but benefits can be hard to measure.

Difficulties with partnership working often include a failure to realise savings and other benefits from the partnership business case, or significant overspends on projects where the public sector has partnered with the private sector. Under the previous use of resources assessments, underdeveloped partnership governance arrangements were often cited as a reason for not awarding higher scores.

Our survey results showed that 89% of respondents agreed (25% strongly) that officers and members were clear on roles and responsibilities when the council works in partnership. The positivity of this response is at odds with previous external assessments and views from the sector. This suggests there may be a gap between aspiration and theory, and reality in practice.

<table>
<thead>
<tr>
<th>Response</th>
<th>Percentage</th>
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</thead>
<tbody>
<tr>
<td>Strongly agree</td>
<td>25%</td>
</tr>
<tr>
<td>Tend to agree</td>
<td>64%</td>
</tr>
<tr>
<td>Tend to disagree</td>
<td>10%</td>
</tr>
<tr>
<td>Strongly disagree</td>
<td>1%</td>
</tr>
</tbody>
</table>

*When working in partnership, members and officers are clear about their roles and responsibilities individually and collectively in relation to the partnership and the Council.*
The diversification of public service delivery, as set out in the Government’s Open Public Services White Paper, is likely to see the rise of smaller and less experienced public service providers, with more SMEs, charities and social enterprises entering the market alongside large private sector providers. The White Paper acknowledges that the risk of failure among providers of public services is likely to increase, as minimum standards and expectations required of providers increase, for example, through the use of outcome-based contracts and payment by results. The recent collapse of Southern Cross, and its impact on 31,000 care home residents, brought this increasing governance challenge to wider public attention.

The lack of a formula for success in ensuring effective partnership governance and its importance in maintaining public accountability have long been recognised. Structured collaboration is being explored to help understand and better manage the costs, benefits and risks of partnership working, so that value and outcomes can be maximised. We believe that now, more than ever, councils must ensure they have robust governance arrangements in place and that there is clear accountability between partners. Partnership risk management arrangements need to be robust and audit committees should be clear about what assurances they require.

“Shared responsibility should not mean diminished accountability.”

Audit Commission, Governing Partnerships, Bridging the Accountability Gap, October 2005

Weaknesses in addressing partnership risk

- Failure to understand the extent of their involvement in partnerships or its implications, including their financial and legal liabilities. Partnerships can operate in isolation, duplicating effort and activity. Partners may not be adhering to the standards and protocols expected of them in the corporate sphere.
- Absent or insufficient corporate criteria to enable public bodies to assess whether to form a partnership or participate in one, what the appropriate level of involvement should be and what resources to invest. They may lack formal procedures for assessing the suitability of partners, the legality of the proposed partnership arrangements and standards of financial regularity or conduct.
- Insufficient thought given to planning an exit strategy. Partners should clarify the management of any continuing financial liability, the ownership of assets and arrangements for disposal in order to avoid the risk of future legal disputes, or of the accountable body (often a council) becoming liable by default.
- Lack of clarity on insurable risk, such as indemnity cover for partner members or public liability.
- Lack of formal systems for recording conflicts of interest or for assessing the risks of funding proposals.

Governing Partnerships: Bridging the Accountability Gap, Audit Commission, 2005
Councils have traditionally had less well-developed arrangements in partnership risk management. We believe this will need to improve if councils are to demonstrate appropriate partnership risk management arrangements as part of setting priorities, policy making, financial planning, information sharing and performance management.

For example, there could be a requirement for separate risk registers to be maintained for each significant partnership, or the establishment of a member sub-group to monitor partnership arrangements, particularly during the set up and early operational stages. AGS should explicitly record the governance framework and assurances received for significant partnerships.

Where services are delivered with or by third party organisations, audit committees must be satisfied that management has obtained appropriate assurance on factors such as service quality and continuity, value for money and probity.

Cultural and behavioural aspects of partnership working are equally as important as structures and processes in ensuring effective partnership governance. Reaching a common understanding of the right behaviours is a key challenge for organisations coming together to deliver public services.

As councils work more in partnership, we suggest that partners invest time up front in working together to understand their respective cultures and how these could affect the governance and performance of the partnership. This is often best done through on-going team-to-team sessions facilitated by independent experts.

Audit committee checklist for partnership governance

Do we have the necessary assurance around:

- clarity over who the council’s significant partners are?
- appraisal processes to ensure that detailed partnership business cases are developed and scrutinised effectively?
- clarity of anticipated outcomes, savings and other benefits from the partnership in a document that has been signed off by all partners?
- a realistic assessment of the risks and potential conflicts, and agreement on how they will be managed?
- the performance management framework to monitor delivery and provide accurate and timely management information for transparent and informed decisions?
- clear contractual arrangements, for example, setting out how risks and rewards are to be shared between partners?
- compliance with all legal and statutory requirements?
- compliance with all ethical standards, such as registration and declaration of partners’ interests?
- having strong client-side experience, with clear ownership and oversight of delivery, including effective contract and project management arrangements?
- a properly constituted partnership board with effective and clear leadership?
- contingency plans to ensure continuity of service in case something goes wrong?
The level of fraud against local government in 2011 is estimated at 10 times greater than that actually detected. To stem this tide, we believe councils should follow established anti-fraud and corruption guidelines.

In its Annual Fraud Indicator 2011, the National Fraud Authority estimated that fraud against the public sector totalled over £21 billion a year, with local government losing over £2 billion.

The Audit Commission’s statistics demonstrate the commonly accepted view that fraud and attempted fraud increase in difficult economic times. We used our survey to gather the views of senior officers and members on how well they recognised, and were dealing with, the increased fraud risk and the implications of the Bribery Act.

Our results showed that 92% of respondents believed their councils were aware of, and had effectively responded to, the heightened risk of fraud and corruption sparked by the recession. A significant proportion said they ‘strongly agree’ with this statement. Just 8% (mainly chief executives and directors of governance) said they ‘tend to disagree’.

We are aware of the current heightened risk of fraud and corruption and have effectively put in place additional preventative and detective controls to address this.

<table>
<thead>
<tr>
<th>Fracture Type</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Housing tenancy fraud</td>
<td>£900m</td>
</tr>
<tr>
<td>Procurement fraud</td>
<td>£855m</td>
</tr>
<tr>
<td>Payroll and recruitment fraud</td>
<td>£152m</td>
</tr>
<tr>
<td>Council tax fraud</td>
<td>£90m</td>
</tr>
<tr>
<td>Blue Badge Scheme abuse</td>
<td>£46m</td>
</tr>
<tr>
<td>Grant fraud</td>
<td>£43m</td>
</tr>
<tr>
<td>Pension fraud</td>
<td>£8m</td>
</tr>
</tbody>
</table>

This result indicates that councils are very positive about their anti-fraud arrangements. The Audit Commission’s figure of £185 million of fraud detected is a significant amount. However, this is only 10% of the £2 billion of fraud committed against councils. In this context, any proposals to reduce control and investigation resources may be counter-productive. We would suggest that increased resources could potentially be funded by heightened fraud detection and prevention.
The Audit Commission report, Protecting the Public Purse, examines key fraud risks and good practice and makes recommendations for local government. It also contains a useful governance checklist to assess anti-fraud arrangements, with guidance on:

- general matters, such as policies, procedures, staffing, awareness and working with other organisations
- fighting fraud with reduced resources
- current risks and issues, such as tenancy, procurement, recruitment, personal budgets and benefits.

We believe more could be done to prevent and detect fraud in local government. Given the heightened risk of fraud, we recommend councils assess their arrangements using the Audit Commission checklist and DCLG 10-point plan (see opposite). Constructive, external challenge may help when carrying out this process.

The difficulty in recovering money lost through fraud causes much frustration among public sector bodies. While the level and speed of recovery can be complicated by criminal proceedings, councils must be confident they are doing all they can to recover their losses, quickly. This has the benefit of adding to the deterrent effect.

Depending on the level of resource and expertise in councils, it may be appropriate to seek specialist help to recover misappropriated funds and mitigate losses from fraud. This can help to:

- reconstruct financial information
- quantify the amount of funds involved
- trace the proceeds of the fraud
- identify recoverable property
- assist in securing the recovery of amounts stolen.

Councils should also maintain sufficient records of how much has been saved compared to the cost of investigating fraud and pursuing recovery.

The Department for Communities and Local Government press release, 11 May 2011
The Bribery Act

In our survey, 92% of respondents agreed, with over half ‘strongly agreeing’, that their councils were aware of the implications of the Bribery Act and had taken action to minimise the risk of investigation or prosecution. As with fraud, chief executives and directors of governance scored lower.

Corruption risk through involvement in large-scale procurement and tendering needs careful management. With the emphasis on localism and outsourced service provision, new relationships are continually being forged between councils and third-party and private sector organisations.

Joint prosecution guidance from the Serious Fraud Office and the Director of Public Prosecutions stresses that the Act is not limited to commercial bribery, specifically mentioning influence on decisions by councils and members. So far, the Bribery Act has not been used extensively in the public sector, indicating success for the sector and those supporting it in spotting the risk and taking advice. However, the first conviction under the Bribery Act, in November 2011, where a public sector employee was jailed for six years after admitting he received a £500 bribe, serves as a reminder for councils to keep their arrangements under review.
Fraud, corruption and the Bribery Act

The Bribery Act – some essential steps

• Respond now to the Act if your council has not yet done so. It can take longer than you think
• Consider using specialist external help, for example to perform a corruption risk assessment
• Introduce, revise or align policies and procedures to mitigate risks
• Train staff most exposed to corruption risk
• Keep a record of all you do in responding to the Act.

Questions to ask yourself

• Has the council prepared a strategy for responding to the Bribery Act?
• Has a named individual within the council been charged with implementing the requirements of the Act and investigating reports of possible corruption?
• Have we performed a corruption risk assessment (CRA)?
• Are our anti-bribery policies and procedures aligned to the CRA?
• Do our policies and procedures fully address facilitation payments, gifts, entertainment, corporate hospitality and charitable donations on a global basis?
• Do we clearly and regularly communicate the council’s strategy and policies on anti-bribery and corruption to all staff, including contractors?
• Is there an anti-corruption training programme for the executive, all managers and staff?
• Do we have an effective compliance monitoring programme, which provides the requisite assurance?
The explanatory foreword

Last year’s explanatory forewords ranged from one to 59 pages and varied widely in content and approach. We believe that officers and members should ensure theirs is concise, comprehensive and accessible and serves to enhance council accountability.

The importance of the explanatory foreword

The explanatory foreword to the accounts is particularly important in local government as there are no mandatory annual reports to provide a full picture of how councils are doing, in financial and non-financial terms. This is especially so now, as stakeholders become increasingly interested in how councils are spending taxpayers’ money.

However, council accounts, with their coverage of complex multi-purpose operations and fulfilment of additional statutory statements, are not easily accessible to the layperson. The introduction of International Financial Reporting Standards (IFRS) in 2010/11 is perceived by many to have made the accounts even longer and more difficult to interpret.

In this context, a good explanatory foreword to help the reader easily understand the accounts is essential. The 2010/11 Code of Practice on Local Authority Accounting has 12 recommendations on what to include in the explanatory foreword. These are set out in our analysis of compliance, overleaf.

The explanatory foreword to the annual accounts serves as a clear and concise introduction to the accounts and overview of the financial position of the council.

| Strongly agree | 57% |
| Tend to agree  | 38% |
| Tend to disagree | 5% |
| Strongly disagree | 0% |

The average length of the explanatory forewords we reviewed was nine pages, although they ranged from one to 59 pages. Despite this variation, our survey showed 95% of respondents felt the explanatory foreword served as a clear and concise introduction to the accounts and an overview of the financial position of the council – 57% ‘strongly agreeing’.

Although chief executives and audit committee chairs scored lower than others, the findings suggest that senior council representatives believe the explanatory foreword is fulfilling its primary purpose. However, we question how the shortest forewords achieve compliance and how the longest can be regarded as concise and user friendly.

“The purpose of the foreword is to offer interested parties an easily understandable guide to the most significant matters reported in the accounts. It shall provide an explanation in overall terms of the authority’s financial position and assist in the interpretation of the accounting statements, including Group Accounts.”

Code of Practice on Local Authority Accounting, CIPFA, 2010/11
Our explanatory foreword review findings

The explanatory forewords to the 2010/11 accounts were reviewed against our best practice criteria. These included:

- compliance-based questions taken from the Code of Practice on Local Authority Accounting
- clarity and consistency questions, including internal consistency with the accounts and AGS
- best practice questions from other sectors, including those on wider performance and environmental matters.

A team of graduate reviewers took part, to simulate the views of the informed, but not expert, user. We used the following scoring system:

1. Information totally missing
2. Information partially missing
3. Minimum
4. Enhanced content
5. Standard setting

Compliance

A summary of our findings for each set of compliance questions is set out below:

<table>
<thead>
<tr>
<th>Category</th>
<th>Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Explanation of statements</td>
<td>3.0</td>
</tr>
<tr>
<td>Financial information</td>
<td>2.4</td>
</tr>
<tr>
<td>Material assets/liabilities</td>
<td>2.3</td>
</tr>
<tr>
<td>Pensions changes</td>
<td>2.9</td>
</tr>
<tr>
<td>Material charges/credits</td>
<td>2.3</td>
</tr>
<tr>
<td>Accounting policies</td>
<td>2.8</td>
</tr>
<tr>
<td>Change in functions</td>
<td>2.1</td>
</tr>
<tr>
<td>Current borrowing</td>
<td>2.4</td>
</tr>
<tr>
<td>Sources of funding</td>
<td>2.3</td>
</tr>
<tr>
<td>Significant provisions</td>
<td>2.1</td>
</tr>
<tr>
<td>Post-report events</td>
<td>1.9</td>
</tr>
<tr>
<td>Impact of economic climate</td>
<td>2.6</td>
</tr>
</tbody>
</table>
With a maximum score of 5, an average of 2.4 suggests that disclosure is providing close to the minimum to fulfil compliance needs, rather than seeking to provide the reader with an easily understandable guide to significant matters. Explanations of the statements and significant changes in accounting policies are among the highest scoring areas, but the scores of around 3 do not suggest clear unequivocal guidance.

The lowest average score (1.9) was for details of any material events after the reporting date, where many councils made no comment. This will be partly due to an absence of such events in many councils. However, councils failing to update the AGS for events up to the opinion date was also a frequent occurrence, suggesting there is scope for improvement in councils’ consideration of events after the balance sheet date.

**Clarity and consistency**

For the clarity and consistency questions, the average score was 2.5, suggesting that the explanatory foreword generally was regarded as understandable to the non-expert reader and told a consistent story overall. Reviewers indicated that graphs and tables helped their comprehension.

The weaker areas were around clear reconciliation of figures in the foreword with those in the accounts, consistency with the content of the AGS and coverage of group accounts.

At a number of councils performance was reduced by:

- no explanation for large movements in balance sheet items and in reserves (usable and unusable)
- too much detail on some aspects, such as service expenditure compared to budget
- referencing to notes from the accounts to explain the subject rather than providing a succinct summary of the issue in the foreword.

Providing clarity over the financial position is particularly important in the current financial climate. Our recently published national report on council financial resilience showed that, overall, councils have coped well so far. However, with an average score of only 2.5 out of 5, many councils could provide a clearer explanation of their financial position in the explanatory foreword.

A council’s financial position can be summarised by its balances on usable and unusable reserves, levels of borrowing, movements in net assets, performance on the Comprehensive Income and Expenditure Statement and cash flow. Forewords often failed to give a clear summary of the key financial developments in these areas.
We also believe that a discussion of financial needs and resources should cover the impact of the current economic climate on the council and its services. There was considerable variation in the way councils approached this matter, with examples including:

- no discussion on the savings required in 2011/12
- a useful discussion of the overall macroeconomic situation but little description of the impact of the settlement on the 2011/12 budget
- savings required for 2011/12 quantified and risks summarised
- a full discussion of the impact of the government settlement over the next three years.

**Best practice**

We took the approach to review areas of best practice which, while not mandatory for local government, reflect the requirements to provide real understanding and transparency to the public. They include the sort of information routinely provided in corporate reports.

<table>
<thead>
<tr>
<th>Category</th>
<th>Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overview of authority</td>
<td>1.7</td>
</tr>
<tr>
<td>Use of KPIs</td>
<td>1.1</td>
</tr>
<tr>
<td>Risks/uncertainties</td>
<td>2.2</td>
</tr>
<tr>
<td>Complements the accounts</td>
<td>2.5</td>
</tr>
<tr>
<td>Environmental matters</td>
<td>1.2</td>
</tr>
<tr>
<td>Clear/concise</td>
<td>2.7</td>
</tr>
</tbody>
</table>

For example, we looked at whether councils considered their environmental impact. Under s417 of the Companies Act 2006, a company must include a statement in its business review section that an impact assessment has taken place, and, in 2010, 98% of the FTSE 350 did so. Our research found councils scored an average of 1.2 in this area, indicating that the great majority did not comment on the effect of council policies and actions on the environment.

Many councils provide similar information in other public documents. However, we maintain that good governance includes making key information as accessible as possible to stakeholders. So, if not included in an annual report, we believe the next best place for these best practice disclosures is in an expanded explanatory foreword to the published accounts.
Councils should ensure that explanatory forewords:

- fully comply with the requirement of the Code of Practice, paying attention to the areas we suggest are weak
- are of good quality, ensuring consistency and clear referencing with the figures in the single entity and group accounts
- contain pertinent information the reader would expect to see, for example, detailed discussion around financial resilience in the current climate
- move towards inclusion of wider best practice content around council performance, risks and environmental matters
- are written, reviewed and published with the user in mind, including consideration of language, length and ease of access.

Achieving all this in a document of a manageable length is not easy. Our long experience of reviewing annual reports in other sectors shows a trend of increased compliance but longer documents. These are some signs of a growing focus on quality of information rather than quantity, but the average length of annual accounts for the FTSE 350 is still too long, growing last year by 5% to 135 pages. The NHS is facing this challenge and we believe councils could do the same for their explanatory forewords (and AGS).

Explanatory foreword best practice questions

Does the foreword:

- provide an overview of the council, including services, locations and structures?
- use key performance indicators (KPIs) used to highlight performance across differing aspects of the council?
- explain the major risks and uncertainties facing the council?
- complement, as well as supplement, the annual accounts to enhance the overall disclosure (this will include providing financial and non-financial information about the authority and its performance that is not reported in the annual accounts)?
- include commentary on environmental matters?
- clearly and concisely introduce the reader to the accounts in a way that enables the reader to access the financial statements easily and understand its key messages?

Explanatory foreword – towards better reporting

Our research showed that council explanatory forewords are largely compliant with current requirements. However, the average score of less than 3 across the various assessment categories suggests aspects could be better reported for improved transparency and accountability to stakeholders.

Councils may wish to consider subjecting their explanatory forewords to a fundamental review from a user perspective. This could help councils ensure their explanatory forewords are as helpful and informative to non-experts as they are to those familiar with reading accounts.

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- are of good quality, ensuring consistency and clear referencing with the figures in the single entity and group accounts
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With more than a third of members and senior officers saying that they did not find the accounts helpful, there is a clear message that councils should review the overall usefulness to stakeholders of their accounts.

**Accounts – other survey results**

Well over half (62%) of respondents said they found the accounts helpful in understanding the financial position of the council, but a third, mainly directors of finance and heads of internal audit, disagreed. This contrasts with the results of the explanatory foreword question where there was a 95% positive response.

These findings suggest that councils need to review the overall usefulness to stakeholders of their accounts. Again, this is not a simple task when we consider mandatory statutory statements and the impact of IFRS, but it is an important public accountability issue.

**Top tips for producing helpful accounts**

- **Scheduling** – allow sufficient time in the closedown plan to consider from the outset how best to present the accounts, and properly review and challenge them at the end.
- **User perspective** – keep the reader in mind and regularly ask yourself whether there is anything you could do to make the accounts more clear.
- **Presentation** – be prepared to present information differently and ensure that irrelevant information is removed.
- **Review process** – seek a challenging review from someone who can give an independent user perspective that complements the s151 officer’s review.

**I find the accounts helpful in understanding the financial position of the council**

- 26% Strongly agree
- 36% Tend to agree
- 23% Tend to disagree
- 15% Strongly disagree
Our survey showed that 95% of respondents felt the annual accounts were made available to the public in a timely and easily accessible way, over three quarters ‘strongly agreeing’. Perhaps surprising to note was that audit committee chairs, who are recipients rather than compilers of the accounts, scored lower than others.

The response to the statement around timeliness and usefulness of summary accounts information was also very positive.

We also carried out web searches for annual accounts and, if not successful, asked all councils in our population for their draft accounts before 30 September, explaining the reason for the request. Although no longer formally required, it is good practice to make the unaudited accounts available.

Our results failed to support the high level of accessibility suggested by the survey results as:

- We were not able to obtain 20% of English upper tier and Welsh draft accounts before 30 September (the remainder were available in October).
- Over a quarter of Scottish councils would not release their accounts at 30 October, a month after the statutory accounts deadline.
- A number of councils suggested that we should submit a Freedom of Information request to obtain the unaudited accounts.

The annual accounts are made available to the public in a timely and easily accessible way.

- 79% Strongly agree
- 16% Tend to agree
- 3% Tend to disagree
- 2% Strongly disagree

The summary accounts are made available to the public in a timely way and provide clear and concise key information and messages from the full accounts.

- 43% Strongly agree
- 46% Tend to agree
- 10% Tend to disagree
- 1% Strongly disagree
Public accountability

Better annual reporting and quicker handling of complaints and requests for information could help improve accountability – and win hearts and minds.

Local government is accountable to the public and engages with it in a number of ways – from providing detailed information, on websites and in publications and holding public meetings and consultations to carrying out surveys and setting up user groups. There is also the direct link with the public through elected members.

In recent years, councils have engaged more with the public at a neighbourhood level and, through the transparency agenda, they now publish more information than ever. In addition to the Freedom of Information Act and publication of payments over £500, further recent developments include the DCLG guidance on openness and accountability in local pay.

In this context our survey result was unsurprising: 85% of respondents agreed, with almost half of them ‘strongly agreeing’, with the survey statement that “we have good arrangements for engaging with local people and other stakeholders to ensure robust public accountability”. Results were relatively consistent across positions. This showed overall that senior council figures believed that public engagement was strong.

We have good arrangements for engaging with local people and other stakeholders to ensure robust public accountability.

| Strongly agree | 41% |
| Tend to agree  | 44% |
| Tend to disagree | 15% |
| Strongly disagree | 0% |

After allowing for the common issue from council surveys of ‘like the service, don’t like the council’, the results above, while reasonably good, fell short of councils’ own views of the robustness of their public accountability.

While there is probably a limit to how well councils can ever perform in such public satisfaction scores, based on our research and wider experience, we believe there are areas where accountability could be improved. In particular in annual reporting, including the accounts and AGS, and the management of complaints and information requests.
Annual reporting

Producing an annual report is the best way for councils to make relevant information available to the public. We recommend that all councils do so.

Earlier in this report, we suggested that councils needed to do more to improve the quality and accessibility of their statement of accounts, including the explanatory foreword and AGS. Our review of explanatory forewords was designed to look for best practice content along the lines of the requirements for commercial annual reports and, as described, councils did not perform well.

However, most councils can point to other areas on their website where this information – such as KPIs, analysis of significant risks and environmental reporting – can be found or requested.

The Audit Commission promoted annual reports as good practice through the use of resources framework, although annual reports have never been mandated in local government. Some councils embraced the Audit Commission’s emphasis, producing timely and helpful annual reports. Since the use of resources assessment ended, however, the number of council annual reports has fallen dramatically.

We regret this decline. Our central point remains that producing an annual report is the key way for councils to show their commitment to making all relevant information publicly available in the most accessible way. Produced by 30 September each year, it would include audited summary accounts, a final AGS, an explanatory foreword, KPIs, significant risks, environmental matters and any other information that the council believes stakeholders should see.

As in the large corporate sector and the NHS, there will be a challenge to keep reports comprehensive yet concise. However, we believe it is a challenge worth tackling.

10 principles for good annual reports

1. The annual report and accounts needs to comply with relevant law and accounting standards and give complete and accurate accounting information.

2. The explanatory foreword should be consistent with the accounts. The narrative should explain significant points in the accounts, with no surprises.

3. The annual report should give a clear and balanced account, including an explanation of the council’s business model and the salient features of the financial position and performance, good and bad.

4. It should describe the (genuine) principal risks and uncertainties faced by the council. The reader should be able to understand why they are important, and the links to accounting judgements and estimates should be clear.

5. Where the council has referred to KPIs, these need to be reconciled clearly to main heading figures in the accounts. Any adjustments need to be explained clearly, with the reasons why they have been made.

6. Important messages need to be highlighted and supported with relevant context and not obscured by immaterial detail. Effective cross-referencing needs to be provided and repetition avoided.

7. Language needs to be precise, with complex issues explained clearly. Jargon and boilerplate should be avoided.

8. Items in the annual report and accounts should be reported at an appropriate level of aggregation to convey the essential messages and avoid unnecessary detail. Tables of reconciliations need to be supported by, and consistent with, the accompanying narrative.

9. Significant changes from the prior period in policy or presentation need to be explained properly.

10. The spirit as well as the letter of accounting standards needs to be followed and appropriate disclosures provided to give a true and fair view.
Requests under Freedom of Information (FoI) increased by 20% in 2010. According to a report by the Constitution Unit of University College London’s Department of Political Science, the 353 English councils received 200,000 FoI requests. Findings include:

- a fifth consecutive year of double-digit increase in requests
- the estimated cost to English councils was almost £32 million
- members of the public, journalists and businesses made the most requests
- finance, service delivery and personal information were the top three types of requests
- refusal rates fell from 9.3% in 2009 to 6.3%
- the top three problems with requests were difficult requesters/requests, lack of resources and co-operation from service departments
- the top three ways FoI had improved councils were in openness/transparency/accountability, better records management and improvements to organisation.

In 2010/11 the Local Government Ombudsman in England received 21,840 complaints about councils, an increase of over 20% on the previous year.

In this environment, there is a risk of unintended consequences through councils taking a defensive position. To mitigate against that, councils should consider reviewing their complaints and information-request handling arrangements against best practice (see box).

Managing complaints and information requests

Councils can promote transparency while managing costs and workload by reviewing their handling arrangements against best practice.

Dealing efficiently and effectively with requests and complaints

1. Develop a reputation as a transparent council. Anecdotal evidence suggests that councils viewed as withholding information are more likely to attract the sustained attention of difficult FoI requesters and complainants.

2. As far as possible, deal with people face-to-face to build trust and minimise the risk of misunderstandings and prolonged exchanges.

3. Respond in accordance with your own service standards, for example, on timeliness and level of person responding.

4. Get it right first time by ensuring that departments understand the importance of effective complaint/request management and employ robust checking mechanisms to ensure that information provided answers the question asked.

5. Wherever possible, build a constructive relationship with local press to ensure that reports on the council are accurate and fair and do not give rise to superfluous requests or complaints.

6. Have a clear and reasonable policy on how to deal with serial or vexatious complainants and stick to it.
People

Capacity and capability

With people, behaviour and culture at the heart of effective governance, we believe councils should review the way they develop officers and members.

Of our survey respondents, 80% said their councils had robust arrangements to develop the capacity and capability of their officers and members. However, most ‘tended to agree’ rather than ‘strongly agreed’ and 20% disagreed, making this one of the strongest negative survey results.

When we have carried out developmental work with councils, we have sometimes seen a similar pattern of results – that is, individuals assess organisational arrangements favourably, but the capability of their peers less favourably. The conundrum is: as people, culture and behaviour are at the heart of making governance work, if capacity and capability isn’t being addressed as well as it could be, how can the other results be so positive? This may represent a gap between aspiration and reality.

It is best practice for councils to routinely self-assess the effectiveness of each of the components of their governance framework. To prevent these being tick-box exercises, they should be honest assessments, including the capacity and capability of those involved.

The results of this survey question suggest that roles and responsibilities may need to be revisited and further training and development considered.

We have robust arrangements to develop the capacity and capability of officers and members.

<table>
<thead>
<tr>
<th>Response</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Strongly agree</td>
<td>10%</td>
</tr>
<tr>
<td>Tend to agree</td>
<td>70%</td>
</tr>
<tr>
<td>Tend to disagree</td>
<td>18%</td>
</tr>
<tr>
<td>Strongly disagree</td>
<td>2%</td>
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</tbody>
</table>

Our survey showed that the chief executive was regarded as the top post-holder responsible for driving council governance. Those councils that have abolished the chief executive post will need to consider how to now cover the accountable officer role and ensure proper leadership of governance.
Standards

There was widespread dissatisfaction with the effectiveness of the outgoing standards system and significant concerns from our survey respondents around responses to ethical issues.

Councils have a duty to promote and maintain high standards of conduct by elected and co-opted members. The regulations, though, are currently in a state of flux.

Our survey showed that 78% of senior officers and members believed their standards committee was responding effectively to ethical issues facing the council and was able to demonstrate annually the value it added. However, over one in five did not agree. Directors of finance and directors of governance were more likely to ‘agree strongly’, while chief executives were more likely to ‘tend to disagree’.

With scrutiny, this was the lowest scoring area in our survey. Consistent with our findings, there is widespread recognition that the outgoing system is over complicated and disproportionate, often with excessive time spent on minor matters.

In England, the Localism Act means that the model Code of Conduct is being repealed, along with the abolition of Standards for England and statutory standards committees. There will be a new statutory regime which will feature:

- criminal offences of failure to register, to disclose at a meeting, or to withdraw from a meeting where a member has a relevant interest
- a streamlined process for dealing with alleged breaches, involving initial assessment of the merits of the claim, which should allow increased focus on more serious conduct issues
- local arrangements for dealing with member misconduct.

At the moment, much of the detail is unclear, including:

- whether police will be interested in pursuing declaration of interest matters
- how independent members can be involved without the special provisions of the repealed Act
- how sanctions will work for proven inappropriate behaviour.

We have a standards committee that is effectively responding to ethical issues facing the council and can annually demonstrate the value it adds.

<table>
<thead>
<tr>
<th></th>
<th>Strongly agree</th>
<th>Tend to agree</th>
<th>Tend to disagree</th>
<th>Strongly disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>29%</td>
<td>49%</td>
<td>20%</td>
<td>2%</td>
</tr>
</tbody>
</table>

Under the new system, councils must determine local arrangements for voluntary codes of conduct, setting up forums for investigating complaints and dealing with persistent misconduct and arrangements concerning the new criminal implications. We recommend that councils consider this together, rather than in isolation, and to seek legal advice.
Gender diversity

On average, 28% of cabinet members are female, but women lead only 12% of councils. We believe that reviewing selection methods could ensure promising candidates are not missed in future.

The scarcity of women on UK boards has been the focus of considerable debate. Our report on governance in the FTSE 350 found that only 10% of directors in the FTSE 350 are women. There are only two women chairs and women in executive director posts only represent 6% of the FTSE 150. In his review, Lord Davies recommended that FTSE 100 companies increase female representation on boards to at least 25% by 2015.

The NHS fares better. Our 2012 NHS governance report showed that 35% of voting board members in trusts and foundation trusts are women.

Although local councillors are elected, not appointed, gender diversity is as important in local government as in any other sector. However, the proportion of women leaders is low, and there are no targets or recommended levels set for local government.

Only 12% of English upper-tier councils have a woman leader, although 28% of cabinet members and 31% of all councillors are women. Female representation on the cabinet is at similar levels in Scotland and Wales.

While local authorities have little influence over the proportion of elected female councillors, our findings suggest councils should review internal processes for selecting cabinet members and leaders to ensure they are drawing from a truly diverse membership. We will review wider aspects of diversity in future reports.

“The search for board candidates should be conducted, and appointments made, on merit, against objective criteria and with due regard for the benefits of diversity on the board, including gender.”

UK Corporate Governance Code, Supporting Principle B.2
Appendix A

Governance roundtable attendees

Adam Broome  Director of Corporate Support, Plymouth City Council
John Bullivant  Chair, Good Governance Institute
Jessica Crowe  Executive Director, Centre for Public Scrutiny
Paul Dossett  Partner, Grant Thornton
Steve Freer  Chief Executive, CIPFA
John Golding  Partner, Grant Thornton
Andrew Holden  Chair, HFMA London
Sarah Howard  Partner, Head of Local Government, Grant Thornton
Paul Hughes  Director, Public Sector Governance Lead, Grant Thornton
Roger Kershaw  Strategic Director Resources, Derby City Council
Rob Leak  Chief Executive, London Borough of Enfield
Simon Lowe  Partner, Grant Thornton Governance Institute
Jon Roberts  Partner, Grant Thornton
Maryellen Salter  Assistant Director of Finance, Audit and Risk Management, London Borough of Barnet
Mike Suffield  Director, Future of Local Audit, National Audit Office
Appendix B

NHS report highlights

Audit and assurance
• FTs (95%) and the FTSE 350 (99%) are comparable, in having a very high proportion describing the work of the audit committee. Trusts at 37%, however, have some way to go.
• The latest revision of the NHS Audit Committee Handbook provides a push for audit committees to get involved in driving the more effective use of clinical audit in improving governance.
• An effective internal audit function serves as the eyes and ears of the audit committee, providing an objective assurance programme giving the audit committee comfort that good governance is in place. However, with only 43% of trusts and 71% of FTs referring to an effectiveness review, there is room for improvement.
• A substantial number of trusts (89%) and FTs (74%) fail to confirm that the external auditor’s objectivity and independence is maintained when, on average, the value of non-audit fees is equivalent to 13% of a trust’s, and 51% of an FT’s, audit fee.

Boards and committees
• 65% of trusts and 14% of FTs fail to adequately explain their model of working. There is a lack of transparency on the overall board governance arrangements that leaves readers of the annual report uninformed and therefore uncertain whether these arrangements really are effective.
• 90% of trusts and 27% of FTs gave no information as to board/committee attendance throughout the year. We are therefore left unsure whether a sufficient breadth of committee members were given the opportunity to contribute or challenge board reports.
• Trusts and FTs should improve the effectiveness and transparency of their arrangements for board evaluation. 79% of trusts and 34% of FTs gave no information about how they review their own effectiveness, let alone obtain an independent view.
• With women holding over a third of posts, they have a strong foothold in NHS boards, showing the way to their corporate cousins and contributing to a more diverse and balanced board than seen in the large corporate sector.
• Only 13% of trusts and 2% of FTs make gifts, hospitality and entertainment disclosures in their annual reports. Trusts and FTs should be demonstrating more publicly their adherence to ethical standards and the requirements of the Bribery Act.

Internal controls
• A better description of the internal control system and the annual review of its effectiveness is required in trust and Foundation Trust (FT) annual reports. Currently only 77% of FTs and 58% of trusts do this.
Appendix B

Risk and performance
• Trusts and FTs need to improve their principal risk reporting in the annual report. 23% of trusts and 10% of FTs fail to describe the risk management process, while 45% of trusts and 13% of FTs make no mention of the principal risks.
• The use of KPIs to help the reader understand how a trust or FT manages and measures the relative success of its strategy, is missing from 39% of FT and 55% of trust annual reports.
• 55% of trusts and 15% of FTs confirm they have signed up to the prompt payments code, although a significant proportion do not make this declaration.

NEDs and Governors
• There is not a clear and transparent majority of NEDs on 41% of FT boards and 33% of trust boards.
• Trusts and FTs need to describe better who sits on key committees and perform an effectiveness review of their arrangements for the appraisal of individual board members.
• Half of FTs provide only boilerplate descriptions of the role of governors, reflecting a residual lack of clarity from FTs around how to maximise the effectiveness of their governor input.

Annual reports
• Trust and FT financial statements and quality reports contain large volumes of information designed to meet regulatory standards that can be difficult to interpret for non-specialist readers.
• Annual reports are often compiled to ‘tick the box’ of regulatory requirements rather than tell a complete story ‘through the eyes of the management’.
• FTs are better at explaining the future development of their business and their performance is closer to the quality displayed in annual reports by the FTSE 350.
• The directors’ assessment of going concern will require greater focus as the impact of the 2012/13 operating framework comes into play.
Appendix C

FTSE 350 report highlights

• Half of all FTSE 350 companies complied with the Combined Code, with another 10% doing so for part of the year.
• Seven FTSE 350 businesses have been in full compliance with the Combined Code throughout the ten years of the review.
• Less than one in ten directors are women, with half of all mid 250 boards exclusively male. 72% don’t disclose their gender policy.
• Seventy per cent of FTSE 350 companies have introduced annual re-election of directors in anticipation of the new UK Corporate Governance Code.
• One in four companies held externally facilitated board evaluations, with 17% more planning a review in the coming year.
• More than half of chairmen’s statements do not discuss governance and only 10% offer real insight into their governance culture.
• Only five companies changed their external auditor and the average tenure of auditor is 34 years.
• Just 25% of companies give real insight into how they monitor and maintain effective oversight of their internal control systems.
• Twenty seven per cent of companies already outline their business model, as required in the new UK Corporate Governance Code.
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