

**The Different Roles of External Audit,
Inspection and Regulation:
A Guide for Public Service Managers**

CONSULTATION PAPER

Public sector audit has a key part to play in safeguarding public money, ensuring proper accountability, upholding proper standards of conduct in public services and helping public services achieve value for money.

The Public Audit Forum was established in 1998. It brings together the public audit agencies on a purely advisory basis to provide a focus for developmental thinking about public audit. It has a remit to build on the existing co-operation between the public audit agencies: to enhance the efficiency and effectiveness of public audit, to provide a strategic focus on issues cutting across their work and to help develop broadly consistent approaches to public audit.

The Public

A key element in the Forum is a consultative forum which draws on the experience and expertise of public auditors, the bodies they audit, the auditing profession and the wider community. The current membership is set out overleaf.

The Public Audit Forum has published the following reports to date:

- The Principles of Public Audit: a statement by the Public Audit Forum (October 1998).
- The Service which Auditees can Expect from Public Auditors: a consultation document (October 1998).
- Implications for Audit of the Modernising Government Agenda: a paper by the Public Audit Forum (April 1999).
- What Public Sector Bodies can expect from their Auditors: a consultation paper (June 1999).
- What Public Sector Bodies can expect from their Auditors (final paper March 2000).
- Propriety and Audit in the Public Sector: a consultation paper (May 2000).
- Data Matching and the Role of Public Sector Auditors: a consultation paper (August 2000).
- Audit Implications of Electronic Service Delivery in the Public Sector (April 2001).
- Propriety and Audit in the Public Sector (final paper August 2001).
- Central Government Audit in the UK after Devolution (January 2002).
- The Whole Truth: Or Why Accruals Accounting Means Better Management (November 2002).

Audit Forum

This report, past publications and other information about the Public Audit Forum are available on its web site at www.public-audit-forum.gov.uk.

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Foreword

Audit, inspection and regulation are important elements in the governance of public services and can - in their different ways - make powerful contributions to improvements in the services provided to users. However, the Public Audit Forum recognises the concerns being expressed in some parts of the public sector that the growing direct and indirect costs of audit, inspection and regulation may at times represent an unnecessary burden on public services.

This guide is designed to clarify the different roles of auditors, inspectors and regulators, to help public service managers understand how these different activities both serve to protect public funds and help to continuously improve the quality of public services. It also seeks to clarify how the different activities relate to each other, by providing working definitions of each activity and highlighting the similarities and differences between them.

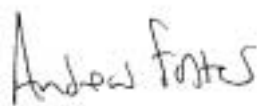
Whilst there may be some similarities between the roles of auditors - in particular performance auditors - inspectors and regulators, they represent distinct, but complementary activities. Recognising the concerns expressed by public bodies and their management, auditors, inspectors and regulators across the public services are committed to working together to avoid imposing unnecessary demands on public services in meeting their respective objectives.

The world of audit, inspection and regulation is complex and changing. In his Budget statement in April 2002, the Chancellor of the Exchequer announced the creation of two new audit and inspection bodies for the health and social care sectors: the Commission for Healthcare Audit and Inspection (CHAI) and the Commission for Social Care Inspection (CSCI). In the coming months, it is likely there may be further changes in the structures of audit, inspection and regulation in different parts of the public services. However, this guide is concerned primarily with the different functions of audit, inspection and regulation, rather than organisational structures and, as such, we believe is relevant and timely.

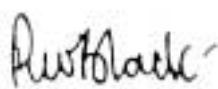
We would welcome comments on the guide from interested parties. Please send any comments you may have to the Secretary of the Public Audit Forum, David Corner at the National Audit Office, 157-197 Buckingham Palace Road, London SW1W 9SP or by e-mail at david.corner@nao.gsi.gov.uk.



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Summary

Audit, inspection and regulation are important elements in the governance of public services and can make powerful contributions to improvements in the services provided to users. However, the Public Audit Forum recognises the concern in some parts of the public sector that the growing direct and indirect costs of audit, inspection and regulation may at times represent an unnecessary burden on public services.

Moreover, we recognise that the world of audit, inspection and regulation is complex. Therefore, this publication is designed to clarify the different roles of auditors, inspectors and regulators, to help public service managers understand how these different activities serve to protect public funds and help to continuously improve the quality of public services. It provides working definitions of each activity and highlights the similarities and differences between them.

For the purposes of this publication, we have used the following terms:

- ◆ **financial audit**, which covers the financial element of auditors' work: the audit of the accounts and the underlying financial systems and processes (including, in specific parts of the public sector, whether public money was spent for the purposes for which it was intended) and the financial aspects of corporate governance, such as internal control and risk management, and probity and propriety;
- ◆ **performance audit**, which is concerned with the performance element of auditors' work: the value for money of services, functions, programmes or specific projects, and the systems and processes put in place by the body to manage its activity and use of resources and to prepare and publish performance information. In local government in England and Wales it also includes auditors' work in relation to best value performance plans;
- ◆ **inspection**, which is the process of periodic, targeted scrutiny to provide an independent check, and to report, on whether services are meeting national and local performance standards, legislative and professional requirements, and the needs of service users;
- ◆ **regulation**, which is the process by which public sector activity and market forces are directed for the public good. It includes the 'authorisation' or 'registration' of bodies to undertake regulated activities and monitoring of their compliance with statutory requirements and professional standards. It may also include the prescription of compulsory activities and price controls.

Public audit comprises both financial audit and performance audit, which are delivered through the national audit agencies and the private firms of auditors they may appoint. Audit, inspection and regulation all provide independent assurance to stakeholders. Financial and performance audit provide assurance on the stewardship of public money and the corporate governance and performance of public bodies. Inspection provides assurance that services are meeting the needs of service users and are achieving levels of performance consistent with national and local performance standards and targets.

Regulators provide assurance that regulated bodies are complying with minimum statutory and professional standards and seek to protect the public and/or service recipients from risks associated with any failure to comply with those standards.

Auditors, inspectors and regulators are all concerned with improving the quality and performance of public services and, to differing degrees, their underlying financial and general management systems and processes.

In some areas there are similarities between performance audit and inspection (particularly in relation to best value in local government in England and Wales). But the key difference between performance audit and inspection is that while inspectors normally examine particular services in terms of professional and service standards, performance auditors are concerned with the organisation's arrangements to secure the best use of resources, as part of public auditors' wider responsibility to report on the stewardship of public money. From their different perspectives, both performance audit and inspection take into account the needs of service users.

All auditors, inspectors and regulators must have relevant specialist professional and managerial experience. They all take account of risk and materiality and/or significance in planning the focus of their work.

While auditors and inspectors rely mainly on the publication of findings to drive change and improve performance, regulators have executive powers to secure compliance. Some inspectors also have the power to recommend the transfer of functions or even prevent bodies from operating where standards are deemed to be unacceptably low. However, where inspectors exercise these powers they could be seen to be acting as a regulator of the body under review. In certain circumstances, some of the national audit agencies and their appointed auditors may also exercise regulatory powers.

Whilst there are some similarities between the roles of auditors, inspectors and regulators, they are distinct, but complementary, activities. Across the public services, auditors, inspectors and regulators are committed to working together to avoid imposing unnecessary demands on public services in meeting their respective objectives.

Introduction

1. Audit, inspection and regulation are important elements in the governance of public services and can make powerful contributions to improvements in the services provided to users. However, the Public Audit Forum recognises the concern in some parts of the public sector that the growing direct and indirect costs of audit, inspection and regulation may at times represent an unnecessary burden on public services.
2. Moreover, we recognise that the arrangements for audit, inspection and regulation of public services are complex. Thus, whilst it is possible to distinguish the different functions, it is not so easy to classify the bodies which carry out these functions. For example, the Audit Commission carries out both audit and inspection functions in relation to local government in England and Wales, while the Housing Corporation carries out both inspection and regulatory functions in relation to registered social landlords in England.
3. Therefore, this publication is designed to clarify the different roles of auditors, inspectors and regulators, to help public service managers understand how these different activities serve to protect public funds and help to continuously improve the quality of public services. It provides working definitions of each activity and highlights the similarities and differences between them.

What is external audit?

4. The term 'audit' is increasingly coming to be used in a generalised sense, to mean any form of scrutiny or review of systems, processes or outputs. However, in the sense in which it has more traditionally been used, audit is the process by which the annual accounts of public and private sector bodies are subject to external scrutiny to provide independent assurance that they have been prepared in accordance with relevant legal and professional standards and give a 'true and fair' view of the financial performance and financial position of the audited body.
5. However, it is one of the basic principles of audit in the public sector, as set out in the Public Audit Forum's publication 'The principles of public audit', that the scope of the audit should be understood to go beyond giving assurance on the accounts, to include examination of aspects of corporate governance and the use of resources (commonly described as 'value for money'). To highlight the differences between audit, inspection and regulation, it is helpful to distinguish between two principal elements of the audit: the financial element of the audit (**'financial audit'**) and the performance element of the audit (**'performance audit'**). In practice, the national public audit agencies promote an integrated approach to delivering the different elements of this 'wider' public audit, which includes both financial and performance audit, whereby work in relation to one element informs work in relation to the other, and vice versa.

6. Financial audit covers the audit of the accounts and the underlying financial systems and processes (including, in specific parts of the public sector, whether public money was spent for the purposes for which it was intended) and the financial aspects of corporate governance, such as internal control and risk management, and probity and propriety. Essentially, it provides assurance that public money has been safeguarded and accounted for properly.
7. Performance audit is concerned with the value for money of services, functions, programmes or specific projects, and the systems and processes put in place by the body to manage its activity and use of resources and to prepare and publish performance information. In local government in England and Wales it also includes auditors' work in relation to best value performance plans.
8. Public audit, comprising both financial audit and performance audit, is carried out by the national audit agencies and the private firms of auditors they may appoint. These agencies are the National Audit Office (on behalf of the Comptroller and Auditor General and the Auditor General for Wales), Audit Scotland (on behalf of the Auditor General for Scotland and the Accounts Commission), the Audit Commission for Local Authorities and the National Health Service in England and Wales, and the Northern Ireland Audit Office (on behalf of the Comptroller and Auditor General for Northern Ireland). The remit of these different agencies is set out in Annex A.
9. Performance audit may take the form of national studies by the national audit agencies themselves. Annex B gives just a few examples from the wide range of performance audit reports produced by the national audit agencies. In England and Wales, auditors appointed by the Audit Commission will carry out local performance audit work, as part of their statutory responsibilities in relation to the use of resources and, in local government, best value performance plans. Such work may take the form of reviews of aspects of audited bodies' performance management arrangements, or of specific services and functions. In carrying out this work, they may apply audit tools developed by the Commission, follow up locally the Commission's national study reports or develop 'bespoke' local studies to address specific issues at particular bodies.
10. Both the financial and performance aspects of audit involve reporting on the stewardship of resources. Thus, the national audit agencies usually require auditors, in planning and carrying out their work, to take into account both financial and performance considerations, having regard not only to the business risks relating to a particular service or function, but also to its relative importance to the public and its representatives.
11. In carrying out their work, whether in relation to financial or performance audit, the national audit agencies and their appointed auditors are concerned to improve the financial and general management, and corporate governance of public services, by identifying and disseminating good, and challenging poor, practices and performance.

What is inspection?

12. Inspection is the process of periodic, targeted scrutiny to provide an independent check, and to report, on whether services are meeting national and local performance standards, legislative and professional requirements, and the needs of service users. Inspectors promote accountability by informing the public and government about the current quality of services and their potential for improvement. They also act as a catalyst for change by holding up an external and objective mirror to the inspected body, helping it to identify priorities for improvement, and challenging poor performance. Inspectors also promote good practice through the recommendations in individual inspection reports, which may be developed by observing good practice in other bodies, and by disseminating them more widely in separate, thematic reports. As such, they play an important role in the development of public policy.
13. In most cases, inspectors focus on specific services or professional activities, eg education or social services. The exception to this rule is the Audit Commission which has statutory responsibility for inspecting the broad range of local government services in England and Wales, which are not otherwise subject to inspection by a statutory inspectorate. Increasingly, however, single service inspectorates have been extending the scope of their work to include the organisation's overall corporate governance arrangements, to the extent that they must necessarily impact on the management and performance of the service being inspected.
14. Inspectors consider aspects of the inspected body's management arrangements and processes, but the focus of an inspection is generally on service outcomes and the performance of public services as individual users experience them. As a result, inspectors spend a considerable amount of time in direct observation of staff delivering services and in comparing the reality of service delivery with the aspirations of management.
15. The methodology and criteria on which an inspector's judgements are made are grounded in first hand experience and evidence of what works in improving services. Inspectors also take into account the use of money, people and assets by inspected bodies and promote the economic, efficient and effective use of public resources.
16. Inspections are carried out by national agencies. By way of example, **Table 1** summarises which inspectorate is responsible for the inspection of major public services in England, Wales, Scotland and Northern Ireland.
17. Some inspectorates, such as the Housing Corporation, also have regulatory functions, while the Audit Commission is unique in that it is a public audit agency that also has inspection functions.
18. A summary of the range of functions of some of the major statutory inspectorates is included as Annex C.

Service	England	Wales	Scotland	Northern Ireland
Education	Office for Standards in Education (Ofsted)	HM Inspectorate for Education and Training in Wales (Estyn)	HM Inspectorate of Education	The Education and Training Inspectorate
Social Services	Social Services Inspectorate (SSI)*	Social Services Inspectorate for Wales (SSIW)	Social Work Services Inspectorate (SWSI)	Social Services Inspectorate (NI)
Police	Her Majesty's Inspectorate of Constabulary (HMIC)		HM Inspectorate of Constabulary for Scotland	HM Inspectorate of Constabulary
Housing Associations	The Housing Corporation**	National Assembly for Wales	Communities Scotland	Department for Social Development
NHS (quality of care)	Commission for Health Improvement (CHI)*		Clinical Standards Board for Scotland	Department of Health, Social Services and Public Safety

* In April 2002 the Government announced its intention to establish two new audit and inspection bodies for the health and social care sectors: the Commission for Healthcare Audit and Inspection (CHAI) and the Commission for Social Care Inspection (CSCI). The new organisations will inter alia absorb the functions of the SSI and CHI. CHAI will also take over the Audit Commission's responsibility for national 'value for money' work. The National Assembly for Wales has yet to announce its proposals for arrangements in Wales.

** In October 2002, the Government announced its intention to establish a new, single Housing Inspectorate under the auspices of the Audit Commission, which will be responsible for the inspection of both local authorities and housing associations.

What is regulation?

19. The term 'regulation' is used by some commentators to describe the overall framework of external review of public sector and regulated private sector bodies. In this publication 'regulation' is used more specifically to mean the process by which public sector activity and market forces are directed for the public good. It includes the 'authorisation' or 'registration' of bodies to undertake regulated activities and monitoring of their compliance with statutory requirements and professional standards. It may also include prescription of compulsory activities and price controls.

20. Regulators are established by government with statutory powers, for example to prevent bodies that persistently fail to comply with minimum standards from remaining in operation. In extreme cases, they may also have the power to prosecute. The availability of such sanctions enables regulators to compel bodies to take certain actions. Such powers are not formally available to auditors and inspectors, who normally are confined to a reporting role.
21. However, some inspectors do have the power to recommend the transfer of functions or even prevent bodies from operating where standards are deemed to be unacceptably low. Where inspectors exercise these powers they could be seen to be acting as a regulator of the body under review. In certain circumstances, some of the national audit agencies and their appointed auditors may also exercise regulatory powers.
22. In some cases, Ministers may act as regulators in exercising their statutory powers to intervene to direct public bodies to carry out certain courses of action in cases where there is evidence of serious failure in the delivery of services. This may include the power to transfer functions to another public sector body or to a private sector provider.
23. While public audit and inspection apply primarily to public sector organisations, public sector regulators may also be responsible for the authorisation or registration and independent scrutiny of private sector bodies that are in receipt of public funds, or which exercise specified public functions, such as the Housing Corporation in respect of registered social landlords in England and Communities Scotland in respect of all social landlords (including local authorities) in Scotland. Funding bodies, such as the Learning and Skills Council in England, may also sometimes have regulatory functions. However, the regulation of wholly private sector activities by inspectorates such as the Financial Services Authority (FSA), OFWAT or OFTEL is outside the scope of this publication.

Independence

24. The independence of auditors, inspectors and regulators in the public sector from the bodies under review is crucial in ensuring that public bodies are accountable for their performance in terms of both stewardship of public money and the delivery of high quality services. Such independence, together with their perceived operational independence (whether formal or not) from government, ensures that these agencies can 'speak as they find' and 'without fear or favour' in a wholly objective way. It serves to reinforce the authority of their findings and the assurance they provide to stakeholders and the public, and is crucial for public confidence in their processes and findings. The independence of the national audit agencies and the auditors they appoint is reflected specifically in their statutory powers and duties.
25. The nature of the relationship between external review agencies and government depends upon the statutory framework under which they were established. The Comptroller and Auditor General is an Officer of Parliament and the National Audit Office (NAO) is completely independent of the Government. The Audit Commission and the majority of national inspectorates and regulators are statutory, non-

departmental public bodies (NDPBs) and enjoy considerable independence from government, even though their boards are appointed by the Secretary of State of the relevant sponsoring government department(s) and they are accountable to the sponsoring department(s) for their financial and operational performance. In Scotland and Wales, the Auditor General is independent and is not subject to the control of any member of the Scottish Executive or Scottish Parliament, or the National Assembly for Wales. The Accounts Commission is a separate body which is responsible for the audit of local government in Scotland. Its members are appointed by Scottish Ministers, but it acts independently of both central and local government. In Northern Ireland, the Comptroller and Auditor General for Northern Ireland is independent of the Assembly, Ministers and Departments.

26. Inspectorates may be part of the government department responsible for the service area they are inspecting. For example, in England, the Social Services Inspectorate is part of the Department of Health and the Chief Inspector is the principal professional social services adviser to Ministers, while in Scotland, the Chief Social Work Inspector is part of the Education Department, providing professional advice on social work issues to the Departments of Health, Education and Justice. In Northern Ireland, the Social Services Inspectorate is a professional group within the Department of Health, Social Services and Public Safety, which supports Ministers, the Department and others working in the field of social care.
27. OFSTED is a non-ministerial government department and Her Majesty's Chief Inspector (HMCI) has a statutory responsibility to keep the Secretary of State for Education and Skills informed about the quality of education provided by schools in England.
28. Chief inspectors may be directed by the relevant Minister to carry out work in a particular area, but they exercise their functions as independent bodies.

Assurance

29. One of the primary purposes of public audit, inspection and regulation is to provide assurance to key stakeholders. Public audit, comprising both financial and performance audit, provides assurance on the stewardship of public money and the corporate governance of public services. While financial audit provides assurance on the accounts and the financial aspects of corporate governance, such as internal control and risk management, and probity and propriety, performance audit provides assurance on those aspects of corporate governance that relate to performance management and the use of resources, including performance information systems.
30. Inspection provides assurance that services are meeting the needs of service users and are achieving levels of performance consistent with national and local performance standards and targets. In doing so they may also provide assurance on the economy, efficiency and effectiveness with which resources are used in meeting professional and service standards.

31. Regulators provide assurance that regulated bodies are complying with minimum statutory and professional standards and seek to protect the public and/or service recipients from risks associated with any failure to comply with those standards.

Securing improvement

32. Improving and maintaining the quality and performance of public services, and their underlying management systems and processes, is fundamental to the work of the national audit agencies and their appointed auditors, through their primary focus on stewardship of resources, and of inspectors and regulators, through their primary focus on service standards. They all alert bodies to the actions required to address identified weaknesses or deficiencies and monitor compliance with agreed action plans and recommendations. However, auditors in particular must avoid compromising their independence by directing a body as to how it should respond to audit findings or recommendations.
33. Financial auditors will as a matter of course identify and report weaknesses in, or make recommendations to improve, accounting and reporting practices, financial systems and processes, internal controls and other financial aspects of corporate governance. In some cases these may be reported to the management of the audited body 'in private', in others - where the issue raised is more significant - they may do so in public.
34. Performance auditors and inspectors judge the current performance of the service, government programme, function or transaction under review against best practice (or, where no external comparator is available, normative criteria) established by national research and evidence collected from previous audits and inspections. Both performance auditors and inspectors are concerned with service outcomes, but while performance auditors focus on the stewardship of resources, inspectors are primarily concerned with professional and service standards. Performance is also increasingly being assessed by reference to national service standards and performance indicators, local performance indicators and benchmarking data. While performance auditors may focus on the potential for achievement of sustained financial savings, both performance auditors and inspectors are concerned with identifying opportunities for measurable improvement in service quality and they both take into account the needs of service users, although from different perspectives.

Skills and experience

35. All auditors, inspectors and regulators must have relevant specialist, professional and managerial experience. Financial auditors will normally be professionally qualified accountants with specialist skills in audit law and procedure, and knowledge of the body of law relating to the audited body.

36. Both performance auditors and inspectors bring their professional and managerial experience to bear in making judgements on service quality and on the potential for services to improve. Both may use multi-disciplinary teams. For example, in its performance audit work the National Audit Office uses multi-disciplinary teams which may include economists, statisticians, academics and individuals with a professional background relevant to the particular study. However, because performance audit involves reporting on the stewardship of public resources, such teams will usually include at least one, or be supervised by, a professionally qualified accountant.
37. Inspectors of particular services will normally have professional expertise and experience relevant to the service in question. However, inspectorates are making increasing use of lay or associate inspectors to provide new insights into the performance of bodies in meeting the needs of users. The Commission for Health Improvement (CHI), for example, routinely includes lay inspectors in its clinical governance review teams, and the Audit Commission uses 'Tenant Inspection Advisers' in its inspection of local authority housing services. Lay inspectors may or may not be users of the service area under review, but they offer a different perspective to the professional and managerial approach that has characterised the traditional approach to inspection.
38. Regulators also make judgements on service quality, but use their specialist knowledge of the service area under review to judge a body's compliance with relevant professional standards and statutory requirements.

Risk assessment

39. Auditors, inspectors and regulators all take account of risk and materiality and/or significance in planning their work programmes, which will in turn reflect their assessment of the adequacy and effectiveness of the body's corporate governance arrangements and of its financial and service performance, as the case may be.

Standards

40. Financial auditors work within a framework of professional auditing and accounting standards. There is no equivalent framework of external professional standards for performance auditors, although the work may be reviewed by external experts. For example, all NAO performance audit reports are subject to extensive external consultation during the audit process and to formal external quality assurance procedures following publication.
41. However performance auditors, inspectors and regulators follow standard methodologies and approaches developed by the individual agencies, which may be reflected in codes of practice, which may be statutory or non-statutory. Increasingly, they also have to work within memorandums of understanding designed to ensure that their work is co-ordinated at those bodies subject to review by a number of external agencies. For example, the Audit Commission has agreed memorandums of understanding with the Local Services Inspectorate Forum in England (which

comprises all local government inspectorates with a responsibility in relation to best value) and the Commission for Health Improvement, which set out the basis for co-operation between auditors and inspectors, and the sharing of information between them. Audit Scotland has similar memorandums of understanding with Communities Scotland, the Benefits Fraud Inspectorate and the Education Inspectorate. It is also working closely with the Scottish police and fire inspectorates.

Reporting

42. An essential output of financial audit is the published opinion on the accounts, which is published alongside the accounts, although private reports and memorandums to the audited body on individual aspects of the audit may also be produced. The wording of the audit opinion, in particular, is prescribed by professional standards and/or statute. Increasingly, the formal opinion on the accounts is supported by a final report (often called the management - or annual audit - letter) from the auditor.
43. In Scotland, for example, all auditors are required by the Auditor General and the Accounts Commission to prepare final reports which summarise areas of concern arising from the audit and action plans to address these concerns. In England and Wales, auditors appointed by the Audit Commission are required to summarise the results and key messages from their financial and performance audit work in an annual audit letter addressed to the audited body. Annual audit letters are normally published by the audited body (NHS bodies are required to consider the letter in a meeting to which the public has access, and in local government the Government has recently introduced a requirement for local authorities to publish the letter). Audit Commission auditors also have special powers to highlight any recommendations in the annual audit letter which the auditor considers require a public response and to issue 'public interest reports' on matters of particular significance - whether relating to the financial or performance elements of the audit - which the auditor considers should be brought to the attention of the public. In Wales, the National Assembly is empowered to call the Audit Commission and its staff to provide information and evidence to the National Assembly or its committees.
44. Performance auditors are less constrained by external standards and statutory rules in reporting the results of their work. However, in local government in England and Wales, auditors appointed by the Audit Commission also have a statutory responsibility to issue a formal report - which is required to be published by the audited body - on authorities' annual best value performance plans (BVPPs). The form and content of these reports are specified in legislation and the Commission's Code of Audit Practice.
45. In central government, the results of financial and performance audits are also reported to the relevant Parliament or assembly and published. The relevant committees of the Parliament or assembly may then decide to carry out their own investigation of the issues raised by the auditor and to publish their own report.

46. Inspectors' and regulators' reports are generally public documents, and some inspectorates may be required by law to publish the findings of an inspection, as is the case with the Audit Commission.

Influencing change

47. The process of external review is a powerful catalyst for change in itself and bodies under review are often required to carry out an internal assessment of their own strengths and weaknesses prior to the commencement of the review.
48. Auditors and inspectors rely mainly on the power of the written word and the publication of their findings to drive change and help improve performance. Auditors can also build on their ongoing relationship with the body to encourage worthwhile change 'behind the scenes', without recourse to the exercise of formal powers.
49. In central government, the NAO reports to Parliament's Committee of Public Accounts, which may carry out its own investigation into the issues raised by the auditor. Similarly, in Scotland and Wales, the Auditor General for Scotland and the Auditor General for Wales report respectively to the Audit Committees of the Scottish Parliament and the National Assembly, which may hold hearings on the matters raised by the Auditor General. In Northern Ireland, the NIAO reports to the Public Accounts Committee of the Northern Ireland Assembly.
50. External auditors of local authorities in England and Wales may recommend to the Audit Commission that a best value inspection should be carried out. They also have the power to refer authorities directly to the Secretary of State or National Assembly for Wales, in cases where the audit of the best value performance plan reveals serious concerns about the ability of the authority to deliver best value. In local government in Scotland, the Controller of Audit can issue a report to the Accounts Commission, which is empowered to hold a public hearing, and following this, can make recommendations to the council or Ministers. The Accounts Commission can also apply sanctions to councillors who are responsible for illegality or loss due to misconduct, including suspension and disqualification from office.
51. Inspectors may use scoring systems to categorise inspected bodies and to encourage them to meet the performance standards of their peers. Some inspectors may also exercise regulatory powers, including the power to refer bodies to Ministers, to recommend the transfer of functions or even to prevent bodies from operating where standards are deemed to be unacceptably low.
52. Auditors and inspectors undertake active monitoring of the progress made by bodies in implementing agreed action plans. Inspectors may use the results of monitoring to determine whether further sanctions should be applied to the body under review. In some cases, they may be required to do so.
53. Regulators may require certain actions to be taken, while auditors and inspectors generally cannot do so directly. Thus, some regulators can impose financial penalties or prevent regulated bodies from continuing in operation by removing their registration or authorisation where standards are deemed to be unacceptably low.

54. Auditors, inspectors and regulators may also advise, and in some cases comment, on the implementation of national policy and make recommendations to government. Their reports can provide valuable information and lessons to government on how services are being delivered on the ground, on good practice as well as poor practice, on 'what works' and the obstacles to improvement, and on the implications for policy.

Joining up audit, inspection and regulation

55. Auditors, inspectors and regulators recognise the concern in some parts of the public sector that the growing direct and indirect costs of external review may at times represent an unnecessary burden on public services. Together, they are taking steps to address these concerns.
56. The national audit agencies have a good track record in working together and using each others' work wherever possible. Practical examples of co-operation and collaboration between the public audit agencies are set out in the Public Audit Forum's publication 'What public sector bodies can expect from their auditors'. One of the purposes of the Public Audit Forum is to promote and enhance such co-operation and collaboration.
57. Audit and inspection are complementary activities, and auditors and inspectors are working together to minimise overlaps and duplication, and share information, to avoid imposing unnecessary demands on public service bodies.
58. In England, the Audit Commission has been carrying out joint reviews of social services with the SSI since 1996 and of local education authorities with Ofsted since 1997.
59. Following the introduction of best value in local government, the Government has established a Local Services Inspectorate Forum, which brings together all those inspectorates in England with a responsibility in relation to best value (the Audit Commission, Ofsted, SSI, BFI, HMIC and HM Fire Services Inspectorate), to consider strategic issues relating to the inspection of best value authorities. It aims to be an effective channel for communication for inspectorates with central government, best value authorities and other interested parties, and to act to increase the effectiveness of inspection on behalf of users, while minimising the demands on inspected bodies. The Forum has already agreed and published a memorandum of understanding on co-operation between auditors and inspectors, agreed a common methodology in carrying out and reporting on cross-cutting best value inspections and is exploring ways in which individual inspectorates can better co-ordinate and, where appropriate, integrate their work at individual bodies. A shared framework for best value inspection, which was endorsed by all the inspectorates represented on the Forum, was agreed and published in 2000. A separate Wales Inspectorate Forum with similar responsibilities has been established by the National Assembly. In Scotland, a Joint Scrutiny Forum brings together all those involved in the external scrutiny of local authorities in order to minimise duplication and make best use of audit and inspection resources.

60. The local government White Paper, 'Strong Local Leadership - Quality Public Services' published in December 2001, reinforced efforts to join up audit and inspection by giving the Audit Commission responsibility for co-ordinating audit and inspection activity at local authorities in England around a process of 'comprehensive performance assessment' (CPA). CPA will result in an overall judgement about how well a local authority is performing and its capacity to improve, drawing on a wide range of information sources, including audit and inspection findings and judgements, and analyses of published performance indicators. Local authorities will be required to respond to this the overall judgement by developing an action plan to address identified weaknesses and secure improvement. This in turn will 'drive' an integrated and co-ordinated, risk-based audit and inspection work programme, the nature and extent of which will vary according to the Audit Commission's assessment of the local authority's current performance and prospects for improvement. Thus, the better performing councils will have 'lighter touch' audit and inspection, while other councils will receive a more rigorous level of external scrutiny and review.
61. In parallel with this development, the Audit Commission is also developing a new approach to joining up audit and inspection, whereby local audit and inspection work will effectively be integrated under a 'relationship manager' who will act as a single point of contact with the local authority and be responsible for:
- ◆ developing a single, combined risk assessment;
 - ◆ developing, agreeing, resourcing, and overseeing the implementation of, and quality assuring, an integrated work programme;
 - ◆ co-ordinating all reporting to the authority, including the production of a joint annual audit and inspection letter.
62. In the NHS, the Audit Commission and CHI have agreed a memorandum of understanding on how they will work together, for example in CHI's local reviews of clinical governance and non-clinical risk management and systematic reviews of national service frameworks and on the Audit Commission's national value for money studies. This memorandum of understanding is complemented by a memorandum of understanding between CHI, the Audit Commission and its appointed auditors, which sets out the basis for co-operation between auditors and CHI reviewers and investigators, and the sharing of information between them.
63. The national audit agencies have also issued internal guidance in order to ensure that, wherever appropriate, their work is co-ordinated with, and complements, the work of both inspectors and regulators. For example, the Audit Commission's Code of Audit Practice requires its auditors to co-operate with, and have regard to the work of, other auditors, inspectors and statutory review agencies, wherever appropriate. It has also signed up to memorandums of understanding on co-operation, and the sharing of information, between its appointed auditors and the Benefits Fraud Inspectorate and the Commission for Health Improvement. The National Audit Office has issued internal guidance on the design of performance audits that encourages dialogue with inspectorates and, where appropriate, joint-

working with them. For example, in its study of the implementation of the National Probation Service's information systems strategy, the National Audit Office undertook joint visits with Her Majesty's Inspectorate of Probation. And in a study of the criminal justice system, the National Audit Office worked with Her Majesty's Magistrates' Court Services Inspectorate, Her Majesty's Inspectorate of Constabulary and the Crown Prosecution Service Inspectorate to develop its methodology.

64. The national audit agencies also work closely with regulators where this is appropriate. For example, both the National Audit Office and the Audit Commission's District Audit service worked closely with the Health & Safety Executive in their joint study of health and safety in NHS acute hospitals in England. The Health & Safety Executive is the enforcing agency for the Health and Safety at Work Act 1974. The visits to hospitals were undertaken by joint teams of the Health & Safety Executive, the National Audit Office and District Audit. A follow-up study, concentrating on hospital staff safety, is now underway, with the additional participation of the Commission for Health Improvement.

Conclusions

65. Audit, inspection and regulation all provide independent assurance to stakeholders. Public audit provides assurance on the stewardship of public money, and the corporate governance and performance of public bodies. Inspection provides assurance that services are meeting the needs of service users and are achieving levels of performance consistent with national and local performance standards and targets. Regulators provide assurance that regulated bodies are complying with minimum statutory and professional standards and seek to protect the public and/or service recipients from risks associated with any failure to comply with those standards.
66. Similarly, auditors, inspectors and regulators are all concerned with improving the quality and performance of public services and, to differing degrees, their underlying financial and general management systems and processes.
67. In some areas there are similarities between performance audit and inspection (particularly in relation to best value in local government in England and Wales). But the key difference between performance audit and inspection is that while inspectors normally examine particular services in terms of professional and service standards, and users' needs, performance auditors are concerned with the organisation's arrangements to secure the best use of resources, as part of public auditors' wider responsibility to report on the stewardship of public money.
68. All auditors, inspectors and regulators must have relevant specialist professional and managerial experience. They all take account of risk and materiality and/or significance in planning the focus of their work.
69. While auditors and inspectors rely mainly on the publication of findings to drive change and improve performance, regulators have executive powers to secure compliance. Some inspectors also have the power to recommend the transfer of functions or even prevent bodies from operating where standards are deemed to be unacceptably low. However, where inspectors exercise these powers they could be

seen to be acting as a regulator of the body under review. In certain circumstances, some of the national audit agencies and their appointed auditors may also exercise regulatory powers.

70. Whilst there are some similarities between the roles of auditors, inspectors and regulators, they are distinct, but complementary, activities. Across the public services, auditors, inspectors and regulators are committed to working together to avoid imposing unnecessary demands on public services in meeting their respective objectives.

Annex A

The responsibilities of the public audit agencies in the UK

Central Government

The National Audit Office (NAO), on behalf of the Comptroller and Auditor General, is responsible for the financial and value-for-money audit of central government expenditure in relation to matters reserved to the UK government, including defence, foreign affairs, social security and central government taxation and all other expenditure by central government departments in England. The NAO is also responsible for auditing the payment of the block grants to the devolved administrations and direct expenditure by the Scotland Office, Wales Office and Northern Ireland Office. The Auditor General for Scotland audits or appoints the auditor to those bodies funded by the Scottish Parliament and audits the accounts of the Parliament. The Auditor General for Wales audits the accounts of the National Assembly for Wales and those organisations funded by the Assembly. The Northern Ireland Audit Office (NIAO) is responsible for the audit of spending by the Northern Ireland Departments and a wide range of public sector bodies including the cross-border authorities created by the Northern Ireland Act 1998.

Local Government

The Audit Commission is responsible for the appointment of auditors (from private firms and its own agency, District Audit) to local government in England and Wales. It also carries out value-for-money studies of these bodies. The Accounts Commission has similar responsibilities in Scotland. In Northern Ireland the appointment of auditors is the responsibility of the Northern Ireland Department of the Environment.

National Health Service

The NAO audits the summarised accounts of the NHS and can carry out performance audit at NHS bodies in England. The NIAO has similar powers and responsibilities in respect of Northern Ireland. The Auditor General for Scotland is responsible for the financial and performance audit of NHS bodies in Scotland and appoints the external auditors of health bodies in Scotland. The Auditor General for Wales can carry out performance audit at NHS bodies in Wales.

The Audit Commission is responsible for the appointment of auditors to Strategic Health Authorities, Local Health Boards, NHS Trusts and Primary Care Trusts in England and Wales and undertakes performance audit studies as well. In Northern Ireland the appointment of auditors is the responsibility of the Northern Ireland Department of Health, Social Services and Public Safety.

Police authorities

The NAO is responsible for the audit of the Northern Ireland Policing Board, although this work is carried out by the NIAO on its behalf, and certain other police forces such as the British Transport Police. The Audit Commission is responsible for the audit of other police authorities in England and Wales. The Accounts Commission has similar responsibilities in Scotland.

Annex B

Performance audit work carried out by the public audit agencies

The public audit agencies carry out a wide range of reviews on ways in which public bodies can improve value for money in the use of resources.

National Audit Office	Auditor General for Scotland	Audit Commission
<p>The Channel Tunnel Rail Link (2001)</p> <p>This report looked at the process by which the former Department of Environment, Transport and the Regions negotiated a restructured PFI deal for the Link. It concluded that the Department had conducted the negotiations well, but stated that the complex financial arrangements agreed during the restructuring would require significant long-term Government support. It also raised questions about the wider economic benefits claimed for the Link, which underpin the case for Government support.</p>	<p>Overview of the NHS in Scotland (2001)</p> <p>The Auditor General for Scotland (AGS) presents an annual overview of the NHS in Scotland to the Audit Committee of the Scottish Parliament. This examines the key issues arising from audits of NHS trusts and health boards in the previous year. The Audit Committee takes evidence from Accountable Officers in the NHS on these issues.</p>	<p>The Way to Go Home - Rehabilitation and Remedial Services for Older People (2000)</p> <p>The report concluded that the rehabilitation services needed to help older people to recover from illness and accidents are often patchy and disjointed. It went on to argue for an approach that looks across professional and organisational boundaries and makes full use of the new financial flexibility available to health and social service providers. The Department of Health responded to the Commission's recommendations by issuing guidance on the establishment of intermediate rehabilitation services.</p>

National Audit Office	Auditor General for Scotland	Audit Commission
<p>Action to improve rail passenger services (2000)</p> <p>This report found that the shadow Strategic Rail Authority and its predecessor organisation the Office of Passenger Rail Franchising had taken action where possible to remedy under-performance by passenger train operators, but that the present franchise arrangements could be improved to secure better performance. The report made a series of recommendations to address the weaknesses it found in the franchise arrangements.</p>	<p>A clean bill of health? A review of domestic services in Scottish hospitals (2000)</p> <p>The AGS has adopted a reporting style which encourages continuous improvement in public services. The initial report on a topic is presented to the Audit Committee as a 'baseline report' which outlines current performance but does not name audited bodies. This is followed up typically 18 months to 2 years later to assess progress. At this stage audited bodies are named and the Audit Committee may take evidence. The first baseline report that Audit Scotland published on the AGS' behalf covered hospital cleaning. This is being followed up currently and a detailed report is due in Autumn 2002.</p>	<p>Money Matters: School Funding and Resource Management (2000)</p> <p>This report looks at recent developments in the way that schools are funded and examines how well schools are controlling and managing their finances. The report presents a series of practical recommendations, backed up by internet-based self evaluation tools, on the actions required by schools, councils and government.</p>

National Audit Office	Auditor General for Scotland	Audit Commission
<p>Supporting innovation: risk management in government departments (2000)</p> <p>This report stated that risk taking which is appropriate can promote innovation and lead to improved value for money for taxpayers. It made practical recommendations to encourage the effective planning and management of risk taking.</p>	<p>Making progress with Best Value (2001)</p> <p>Each year the Accounts Commission publishes a national overview assessing the extent to which Scottish local authorities are improving their management of services under Best Value. This is based on a comprehensive performance management and planning audit carried out in all 32 Scottish local authorities.</p> <p>The new Scottish Parliament building (2000)</p> <p>In addition to planned performance audit studies the AGS may respond to requests to examine specific issues where there is some concern that due procedures have not been followed.</p> <p>An example of this type of study is the AGS' report on the management of the project to provide the new Scottish Parliament building at Holyrood.</p>	<p>Testing Times: A Review of Diabetes Services in England and Wales (2000)</p> <p>While the number of diabetes sufferers is rising rapidly due to increasing obesity and an ageing population, the study found that standards of care in diabetes clinics were often inadequate and that ethnic minority patients were twice as likely to report gaps in their understanding of the disease. To tackle the increasing demand, the report recommended more routine care be provided outside hospital, freeing up specialist diabetes teams to provide expert care where needed, and to support other staff in the community. Following publication of the report, data from the Commission's diabetes audits has been used in developing the National Service Framework and a follow-up project on commissioning diabetes services is underway.</p>

Housing Corporation*	Estyn	Social Services Inspectorate**	Her Majesty's Inspectorate of Constabulary for Scotland	Audit Commission Inspection Service	CHI**
<p>Funding registered social landlords (RSLs)</p> <p>Setting performance standards for RSLs</p> <p>Monitoring adherence to performance standards</p> <p>Taking regulatory action where RSLs fail to meet the required performance standards</p> <p>Encouraging innovation and good practice in housing organisations</p> <p>Publishing performance indicators for large RSLs</p> <p>Reporting annually to Parliament through the Secretary of State on the use of funding allocated to the Corporation</p>	<p>Undertaking inspections and reporting on performance and standards at all levels of pre and compulsory education and training in Wales. A number of these inspections are undertaken jointly with the Audit Commission</p> <p>Promoting improvement through the public reporting of inspection findings and emerging good practice</p> <p>Advising the National Assembly on education policy</p> <p>Assessing Further Education institutions in Wales and inspecting Assembly-funded training and careers companies</p>	<p>Providing policy advice within the Department of Health</p> <p>Managing the Department's links with social services departments and other social care agencies</p> <p>Inspecting the quality of social care services</p> <p>Assessing the performance of local councils with social services responsibilities, including Best Value</p> <p>Carrying out joint reviews of social services departments with the Audit Commission</p> <p>Promoting good practice through the publication of national reports and training</p>	<p>Examining matters concerning or relating to the operation of police forces</p> <p>Providing advice to Scottish Ministers on police matters</p> <p>Examining how police forces deal with complaints made against the police</p>	<p>Inspecting services provided by best value authorities and arms-length housing management organisations to determine how good they are and whether they are likely to improve</p> <p>Considering whether the organisation being inspected has established a rigorous programme of service reviews</p> <p>Referring services to the appropriate secretary of state where there are serious service failures, persistent failure to address inspectors' recommendations or serious failures in corporate governance arrangements.</p>	<p>Independently scrutinising the quality and management of health care for which NHS bodies and service providers have responsibility, through a rolling programme of inspections</p> <p>Reviewing and monitoring local and national implementation of national guidelines, such as National Service Frameworks (NSFs) and National Institute of Clinical Excellence guidance</p> <p>Conducting investigations into serious or persistent clinical problems, and, increasingly, taking on responsibility for overseeing and assisting with external NHS incident enquiries in England and Wales</p>

Housing Corporation*	Estyn	Social Services Inspectorate**	Her Majesty's Inspectorate of Constabulary for Scotland	Audit Commission Inspection Service	CHI**
		Advising Ministers on the exercise of intervention powers in cases where there are serious service failures		Promoting good practice through the publication of national reports on the lessons learned from inspections. Carrying out inspections directed by the relevant Secretary of State	Recommending that the Secretary of State should take 'special measures' where an inspection or investigation reveals significant failings Through the Office for information on health care performance, publishing performance ratings of NHS bodies, co-ordinating national clinical audits and carrying out patient and staff surveys Providing national leadership to develop and disseminate clinical governance principles Reporting annually to Parliament through the Secretary of State

* In October 2002, the Government announced its intention to establish a new, single Housing Inspectorate under the auspices of the Audit Commission, which will be responsible for the inspection of both local authorities and housing associations.

** In April 2002 the Government announced its intention to establish two new audit and inspection bodies for the health and social care sectors: the Commission for Healthcare Audit and Inspection (CHAI) and the Commission for Social Care Inspection (CSCI). The new organisations will inter alia absorb the functions of the SSI and CHI. CHAI will also take over the Audit Commission's responsibility for national 'value for money' work. The National Assembly for Wales has yet to announce its proposals for arrangements in Wales.

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