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Auditor General for Wales

## Discussion Paper: The Governance Challenges Posed by Indirectly Provided, Publicly Funded Services in Wales

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The Wales Audit Office study team comprised Alastair McQuaid and Mike Usher.

# Foreword by the Auditor General

Governance is at the heart of public services. It underpins how resources are managed, how decisions are made, how services are delivered and the impact they have, now and in the future. It also infuses how organisations are led and how they interact with the public. Governance needs to be robust but it must also be proportionate. Well-governed organisations are dynamic and take well-managed risks; they are not stagnant and bureaucratic.

Publicly funded services should be delivered by the organisations best placed to do so. Special-purpose public bodies and external contractors play an important role in Welsh public service provision and deliver many benefits. I encourage well-managed risk taking and recognise good practice wherever I come across it; but quite rightly, the public expects high standards of governance whenever public money is involved. Since I became Auditor General in 2010, I have published a series of audit reports that have focused upon governance failures. This paper includes examples from these reports and among the recurring themes are:

- a) ineffective oversight and monitoring
- b) a lack of transparency
- c) inappropriate conduct
- d) poorly managed conflicts of interest

Frequently, these governance failures have occurred within bodies that deliver public services 'indirectly,' at arms-length from their parent or client body. Many were associated with flawed procurement or disposal processes or were failed grant-funded projects. The impacts have included poor-quality services, losses of public funds, reputational damage and erosion of public trust and confidence in those responsible. The root causes of many of the audit issues that I have had to report on have included:

- a) insufficient consideration of arrangements for oversight and the appropriate balance between autonomy and intervention;
- b) a lack of clarity around how governance arrangements should operate in practice, contributing to reduced transparency and diluted public accountability; and
- c) the absence of a consistent and shared understanding of, and commitment to, standards of ethics and conduct to be observed by all those involved in public service delivery.

Unclear governance arrangements in public services create risk. The sheer diversity of governance arrangements that exist within and between bodies that operate at arms-length increases the inherent risks associated with them. If differences in perception and understanding are not recognised, then associated risks are often not properly assessed and so cannot be well-managed.

Meaningful consideration of the governance of indirectly provided, publicly funded services in Wales has to take account of the changing context within which they operate and the broader concepts that underpin them. It appears to me that there are no easy answers; attempts to impose order risk being inflexible and may constrain innovation. A proliferation of rules can be the enemy of good governance; the simpler and clearer the expectations, the more likely it is that those involved in delivering public services will be incentivised to aspire to them. Solutions must be realistic and must be grounded in the values and standards that remain at the core of public services, which are reflected in the principles of the Well-being of Future Generations (Wales) Act. However, there are opportunities to learn, not only from previous failures, but also from existing good practice and innovative ideas, in relation to accepting and navigating complexity.

This paper highlights learning points from my previous audit work. Its contents are relevant to policymakers, officials, practitioners and academics, as well as those who oversee, provide and receive indirectly provided services that are funded with public money. I hope that by stimulating debate, this paper will help to spread good practice, generate new ideas, support beneficial change and so contribute to the good governance of public services in Wales.

**Huw Vaughan Thomas**  
**Auditor General for Wales**

**October 2016**

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# Executive summary

- 1 Increasingly, public services are delivered through subsidiaries, partners or contractors, rather than directly by central or local government bodies or by the NHS. This paper uses the term ‘indirectly provided’ for such services and aims to encourage debate about the governance implications of emerging trends in indirectly provided, publicly funded services in Wales.
- 2 Such services can be provided by a wide range of public, private and third sector entities under various legal, administrative, collaborative and contractual arrangements. This diversity arises from the ways in which Welsh public services have developed over time and also because the pressures for change are complex and are increasing. Although diversity may reflect flexibility and pragmatism and has many advantages, there is also a danger that it can contribute to confusion and increased risk.
- 3 In Wales, as elsewhere in the UK and across the world, the traditional boundaries between the public, private and not-for-profit (third) sectors are also becoming blurred. Whilst the third sector has always played a significant part in delivering Welsh public services, the growth of third and particularly private sector involvement is accelerating:
  - a) as well as the significant role played by the private sector as a supplier of goods and services to public bodies, private entities are increasingly involved in providing services directly to the public, generating profits for their shareholders;
  - b) private individuals bolster the expertise and capacity of public bodies by participating on boards as non-executives, with responsibility for stewardship of public resources and for commissioning and delivering public services;
  - c) partnerships between organisations in the public and private sectors are used to assist delivery of a wide range of public policies and functions by leveraging-in private sector expertise and resources;
  - d) public bodies are engaging in partnerships with, and outsourcing services to, third sector organisations to supplement core capacity, plug gaps in services and better connect with communities;
  - e) some publicly funded bodies within the third sector are seeking to decrease their reliance upon grant funding and donations by engaging in commercial activities, including by providing paid-for services to businesses and to the public; and
  - f) many public bodies are seeking opportunities to generate income by establishing subsidiary bodies as arms-length companies to engage in trading activities.

- 4 As the public, private and third sectors have become increasingly intertwined in public service delivery, it becomes more of a challenge to ensure consistent application of terms such as: ‘the Welsh public sector’; ‘Welsh public services’; ‘public servants’; and ‘public money’. The scale, direction and pace of these changes also bring with them inherent tensions and contradictions, along with potential for conflicting priorities and for imbalances between risk and reward. Nevertheless, regardless of the legal status of an entity or individual involved in dealing with ‘public resources’ to provide ‘public services’; it is essential that their conduct and behaviour meets the high standards expected by the public.
- 5 In addition to individuals or entities involved in delivering public services, the public also has expectations of those who receive public money for other purposes. Significant public funds are paid to procure goods or services from the private and third sectors, or are advanced as grants or loans to support private enterprises engaged in commercial activities which support public policy objectives such as job creation. Although debate about ethics and conduct in relation to public funds beyond their use for public service provision is important, it is outside the scope of this paper.
- 6 This paper does not seek to assess the governance effectiveness of the Welsh Government, individual arms-length bodies or of contracted-out services in Wales. Neither does it evaluate the relative merits or risks of different models of indirect service provision or provide a manual for establishing new arms-length bodies, entering into partnerships or procuring services. Instead, it explores emerging trends and poses questions. Its objective is to prompt discussion amongst public service leaders and stakeholders about how to identify and learn from existing good practice, recognise potential problems and strengthen governance frameworks in order to ensure that the conduct of public business in Wales by all individuals and entities:
  - a) demonstrates appropriately high ethical standards;
  - b) meets public expectations;
  - c) underpins efficient, economic and effective service delivery; and
  - d) safeguards public resources and the well-being of future generations.

- 7 A debate about good governance in relation to indirectly provided, publicly funded services in Wales is necessary and timely because:
- a) new models for delivering services are being developed. Often these involve bodies at arms-length from government and arrangements for procurement, partnership and co-production, which may limit public scrutiny and accountability.
  - b) with increasing private sector involvement in service delivery, personal interests and the profit motive may come into conflict with public sector values of selflessness, user focus and wider public responsibility.
  - c) the administrative and legislative definitions of ‘public services’, ‘public servants’ and ‘public money’ are inconsistent; creating potential difficulties when applying governance rules and principles.
  - d) the provisions of the Well-being of Future Generations (Wales) Act 2015 (the WFG Act) directly affect 44 Welsh public bodies, but have wider implications for all bodies involved in Welsh public service delivery.
- 8 Whilst recognising the diversity and dynamism of Welsh public services provision, it is essential that governance expectations are clearly and consistently understood by all commissioners and providers of public services. However, compliance arrangements must not be so burdensome as to intrude unnecessarily, constrain innovation, compromise efficiency or undermine sustainability. Instead, they should help to build effective relationships, foster trust, provide clarity, support accountability, incentivise improvement and mitigate risk.
- 9 Governance exists to underpin the provision of excellent public services and the proper conduct of public business; it is not an end in itself, nor should it be seen as a drag or obstacle to effective delivery. On the contrary, well-governed organisations tend to be those which provide excellent public services. Organisations which neglect to establish the proper foundations of good governance will often, sooner or later, find themselves in operational difficulties.

## Exhibit 1: a call to action

### **This paper proposes that:**

An effective approach to the governance of indirectly provided, publicly funded services in Wales should:

- underpin expectations of the standards of ethics and conduct of all individuals or entities using public money to deliver services;
- enable individuals and entities to be held to account for their conduct and behaviour, as well as for service delivery;
- take account of the diversity and complexity of public service delivery systems;
- balance autonomy and timely, appropriate intervention;
- spread learning from good practice; and
- support implementation of the WFG Act.

### **We welcome debate on:**

- how existing good practice and diverse approaches to governance can best inform a coherent and transparent approach to the governance of indirectly provided, publicly funded services for Wales;
- how good governance can be incentivised in indirectly provided, publicly funded services, without stifling innovation;
- how risk and reward can be appropriately balanced, and to what extent should senior pay and private profits be moderated when public money is involved; and
- how implementation of the WFG Act can best influence the ethical governance of indirectly provided, publicly funded services in Wales.

# Part 1

## 1. Creating a shared understanding of the issues

- 1.1. Done well, public service governance should enable an organisation to deliver its objectives effectively and to live up to public service values at the same time. However, some difficulties arise in practice because of the absence of a clearly defined, commonly understood and consistently applied set of key terms and concepts.

### Exploring key terms (1): the ‘Welsh public sector’ and ‘Welsh public services’

- 1.2. Public services are hugely diverse, covering functions ranging from transport, health and education to economic development, culture and the environment. Some of these services are provided by private bodies, although they may use public funds. Not all public services deal directly with the public, some provide intermediate services between public bodies.
- 1.3. The Welsh public sector, in common with the UK as a whole, has evolved over many years, rather than being planned from first principles<sup>1</sup>. Not all bodies providing what are commonly understood to be Welsh public services are devolved to Wales; some Welsh public service providers are not part of the public sector; not all employees of public authorities or bodies in Wales are ‘public or civil servants’; and ‘public funds’ may be used by private organisations to engage in commercial activities. What is more, even within what is generally understood to be the public sector, different governance arrangements apply to central government, local government and health bodies<sup>2</sup>.

<sup>1</sup> The National Audit Office report, **Departments’ oversight of arm’s length bodies: a comparative study**, July 2016, examines differences in arms-length delivery systems across four central government departments.

<sup>2</sup> In April 2015 the Auditor General for Wales published **Governance in the NHS in Wales Memorandum for the Public Accounts Committee** which looked in detail at governance in the NHS in Wales.

1.4. In 2014, the Williams Commission<sup>3</sup> identified the Welsh **public sector** as comprising:

‘...the body of staff directly employed by publicly funded bodies.’

And Welsh **public services** as:

‘...services delivered for the benefit of the public; this can include services delivered through the third sector, social enterprise or that are contracted out.’

The Williams Commission also noted that:

‘There is no clear and agreed definition, however, of exactly what the Welsh public sector is, or which organisations it includes...the sector has evolved and that its structure lacks coherence... is highly complex, and may appear to lack an adequate overall rationale. There are several aspects of this which we believe cause serious problems for the governance of the public sector.’

1.5. In response to the Williams Commission’s report, the Welsh Government has begun listing all of the devolved public bodies in Wales and is also seeking to develop a classification system which categorises bodies according to their legal status and their arrangements for accountability<sup>4</sup>.

1.6. The list of devolved bodies in Wales prepared in response to the Williams Commission draws upon various sources of information, such as bodies that receive a remit letter from the Welsh Government, bodies subject to audit by the Auditor General or investigation by the Public Services Ombudsman, bodies whose members are disqualified from being assembly members, and bodies that are required to lay accounts before the assembly. However, these sources are not consistent with each other. In addition, legal definitions are inconsistent; the term ‘public authority’ is defined differently in the Human Rights Act 1998<sup>5</sup>, the Freedom

<sup>3</sup> The Commission on Public Service Governance and Delivery, **Full Report**, January 2014

<sup>4</sup> Following the Commission on Public Service Governance and Delivery (the Williams Commission) report, the Welsh Government has established a register of public bodies in Wales funded from the budget allocated by the UK Government to Wales (the Welsh Block Grant) which has identified 90 bodies in the main register as well as a further 736 town and community councils. Academi Wales quote an estimate of around 3,000 organisations in Wales ‘that deliver public services and/or manage significant amounts of public money’ [Academi Wales, **The Good Governance Guide: Doing it right, doing it better**, Draft, January 2016].

<sup>5</sup> The Human Rights Act makes it unlawful for any ‘public authority’ to act in a way which is incompatible with the European Convention on Human Rights. ‘Public authority’ includes a court or tribunal and any person certain of whose functions are of a public nature.

of Information Act 2000<sup>6</sup>, by EU law, by case law and by the WFG Act<sup>7</sup>.

Furthermore, the terms often used to describe the various types of public body<sup>8</sup> do not provide clear, mutually exclusive definitions.

- 1.7. The European Union (EU) requires the governments of member states to produce accurate public sector accounts according to an EU classification of entities into public or private sectors. The UK's Office for National Statistics (ONS) applies the EU classification<sup>9</sup>, based upon the level of government control over funding, appointments, and operations, and breaks the UK public sector into three areas:
  - a) central government, which in Wales includes the National Assembly, ministerial departments, non-ministerial departments, executive agencies and also Welsh Government sponsored bodies at arms-length from departments.
  - b) local government, which in Wales includes the 22 Welsh unitary authorities, their subsidiary bodies fire and rescue authorities, police and crime commissioners, national park authorities, community councils.
  - c) public corporations, which in Wales are controlled by the Welsh Government but have substantial financial, commercial and operating independence and derive more than half of their income from the sale of goods or services. Public corporations accounts are not consolidated within the Welsh Government department accounting boundaries.
- 1.8. Some of the public sector entities involved in providing services indirectly are included within more than one of the three ONS classifications and the tendency to establish new bodies on an individualised case-by-case basis has often created weak and inconsistent associations between function and form. For example, housing associations are recognised as public bodies for some purposes but are treated as third sector bodies for funding and accounting purposes<sup>10</sup>; universities

<sup>6</sup> The Freedom of Information Act creates a public right of access to information held by 'public authorities'. Public authorities covered by the act are listed in a schedule which is regularly updated. Wholly owned public companies are covered by the act's provisions.

<sup>7</sup> The Well-being of Future Generations (Wales) Act 2015 lists 44 bodies to which the act's provisions apply. However, the Public Services Ombudsman for Wales' remit extends to a wider range of Welsh public bodies.

<sup>8</sup> The terms 'non-ministerial department' and 'non-departmental public body' are purely administrative.

<sup>9</sup> The ONS classifies organisations for national accounts purposes according to categories set out in the 2010 European System of Accounts.

<sup>10</sup> In September 2016 the ONS announced that Registered Social Landlords (RSLs) in Wales, commonly called housing associations, are to be re-classified as public sector bodies. This decision, based on the amount of Welsh Government control over RSLs, will result in over £2 billion of housing association debt being added to Welsh Government accounts and may restrict the ability of RSLs to access private finance.

are not recognised as public bodies by UK law, although they are by EU law<sup>11</sup>. The situation is confusing for the public, who may not even realise that that some public services in Wales (such as Welsh-language broadcasting, policing and the criminal justice system) are not devolved to Wales.

- 1.9. Importantly, there is no agreed strategic approach to developing governance structures and systems for new public service models that consistently relate function to form and enable all relevant entities and individuals to be held democratically and publicly accountable for:
  - a) how well public resources are used
  - b) how well services are delivered
  - c) what outcomes are achieved
  - d) their conduct and behaviour
- 1.10. The particular form adopted when a new body is established will determine characteristics that influence the degree of real and perceived autonomy, the nature and extent of accountability, the extent and effectiveness of public scrutiny and also legal duties. When establishing a new body it is important to review the proposed form and function together and consider them in relation to resulting characteristics including:
  - a) whether the body's financial transactions and balances are consolidated into government accounts, subject to consideration of materiality, or accounted for separately. All UK companies, including those established by public bodies, are obliged to file annual accounts and other information with Companies House, which is publicly accessible. Subsidiary bodies established as limited liability partnerships are not subject to all of these requirements.
  - b) transparency and challenge; the extent to which the body is subject to public audit by the Auditor General, has its own audit committee, is subject to regulatory oversight and also to statutory provisions that enable public transparency (for example, the Freedom of Information Act 2000). Where a body is established as a charity, it will be subject to scrutiny by the Charity Commission to ensure that it is acting within its charitable objectives and in accordance with the Charities Act 2011.

<sup>11</sup> Further and higher education institutions receive public funding but are not classified as public bodies by law in England and Wales. In Scotland further education colleges are now classified as part of the public sector and, therefore, have less flexibility and autonomy than their counterparts in England and Wales. The Public Accounts Committee of the National Assembly recently identified a lack of transparency in relation to senior executive pay, including in relation to the further and higher education sectors. (National Assembly for Wales, Public Accounts Committee, **Senior Management Pay**, November 2014)

- c) the status of employees; whether the body's employees are civil servants, subject to the requirements of the Civil Service code; or other public sector employees subject to the requirements of a professional body; and whether they are public servants for the purposes of the criminal law.
- d) funding, individually or in combination, through the Welsh Government budget, through request for resources, through grants or grant-in-aid, or by income from fees or charges.
- e) financial flexibility and status in relation to requirement to break-even, treatment of financial surpluses, ability to borrow, tax liability and national non-domestic rates liability.
- f) whether EU directives apply, such as in relation to procurement of goods and services, requiring open tendering<sup>12</sup>.

1.11. At present, there is some uncertainty about how the approach to governance in public bodies required by the WFG Act will be achieved in relation to indirectly provided, publicly funded services. We explore this issue in more detail in [Part 3](#).

'There were a range of legal and practical reasons for RIFW's governance arrangements:

- EU funding rules for the JESSICA programme required that RIFW should sit at arms-length from the Welsh Government (and therefore could not have its own Accounting Officer);
- RIFW investment decisions needed to be commercially based; and
- demonstrable managerial independence from political influence would be vital, particularly when seeking potential private-sector investment partners during the planned second phase of RIFW's existence.'

Source: **The Regeneration Investment Fund for Wales** (RIFW), July 2015

<sup>12</sup> Where public bodies procure goods or services, they are expected to follow EU law. To demonstrate that good value for money is achieved from public funding, EU law requires public bodies to advertise contracts above a certain limit in the Official Journal of the European Union. Although commercial, private sector bodies are not covered by EU procurement law, they are expected to use fair and open practices, including competitive tendering, when letting contracts related to public services and public funds.

- 1.12. Whilst this situation rightly allows for flexibility and pragmatism, it can sometimes undermine the consistent application of principles and compliance with standards, rules and guidance. It leads to significant and increasing levels of value for money and reputational risks to the Welsh Government associated with services provided to, and on behalf of, public bodies in relation to:
- a) service models: some delivery models such as consortia (and the legal basis for them) may inhibit transparency and dilute accountability.
  - b) ethical standards: the Welsh Government expects the highest ethical standards of itself, its subsidiaries and indeed all who are involved in delivery of public services in Wales; however, where private entities and individuals are involved, personal interests and the profit motive may conflict with selflessness, user focus and wider public responsibility.
  - c) oversight: the absence of clear and consistent guidance creates confusion in the minds of public officials as to the scope and nature of their responsibilities for overseeing the activities of arms-length providers of public services.

‘The history of the Welsh Government’s management of its relationship with AWEMA raises a more general question about how the Welsh Government can best exercise due diligence to satisfy itself that each of the organisations it funds operates in accordance with principles of good governance, while not interfering in the running of those organisations. This is not just about being able to demonstrate regular monitoring activity. It is also about ensuring that monitoring activity is appropriately targeted, proportionate and that it leads to robust action in response to any issues of concern.’

Source: **The Welsh Government’s relationship with the All Wales Ethnic Minority Association** (AWEMA), October 2012

‘...This degree of active involvement by the observer in the conduct of RIFW’s business potentially jeopardised the arms-length status of RIFW and also may have created the impression of tacit Welsh Government approval for the terms of the sale in the minds of the RIFW Board members and their advisors.’

‘A review commissioned by the Welsh Government has identified weaknesses in the governance arrangements that it established for RIFW that are also relevant to other arms-length agencies.’

Source: **The Regeneration Investment Fund for Wales** (RIFW), July 2015

## Exploring key terms (2): 'public service governance'

- 1.13. Governance relates to how authority is exercised in pursuit of the body's objectives and also to how those who exercise authority are held to account for how they have exercised it by those who have entrusted them with assets and resources. A range of regulation in areas such as employment, health and safety, environmental and social responsibility affects both public and private sector bodies and so governance systems in both sectors need to ensure compliance.
- 1.14. However, governance, the arrangements associated with it and how effective governance can be demonstrated are generally broader and more complex matters for public service bodies than in private organisations. This is because public bodies are usually subject to wider forms of accountability to a variety of stakeholders (including parliaments, governments and taxpayers), than the directors of private companies owe to their shareholders and the wider community under Company Law.
- 1.15. The Chartered Institute of Public Finance and Accountancy (CIPFA) defines governance as:  
'Governance comprises the arrangements put in place to ensure that the intended outcomes for stakeholders are defined and achieved.'<sup>13</sup>
- CIPFA states that:  
'To deliver good governance in the public sector, both governing bodies and individuals working for public sector entities must try to achieve their entity's objectives while acting in the public interest at all times.  
'Acting in the public interest implies primary consideration of the benefits for society, which should result in positive outcomes for service users and other stakeholders.'
- CIPFA describes **public service governance** as:  
'How public 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. It comprises the systems and processes, cultures and values, by which public bodies are directed and controlled and through which they account to, engage with and, where appropriate, lead their communities.'
- 1.16. The Independent Commission on Good Governance in Public Services<sup>14</sup> defined public service governance as:  
'...the leadership, direction and control of organisations... the action, manner, or fact of governing; government... the exercise of authority through formal and informal traditions and institutions for the common good.'

<sup>13</sup> CIPFA/IFAC, **International Framework: Good Governance in the Public Sector, 2014**

<sup>14</sup> Quoted in the Commission on Public Service Governance and Delivery (the Williams Commission), **Full Report**, January 2014.

- 1.17. From a public audit perspective, the three pillars of public service governance are:
- a) **regularity**: acting reasonably<sup>15</sup>, fairly and lawfully within rules, powers and delegated authority;
  - b) **propriety**: conforming to standards of public conduct, behaviour or morals, including acting with integrity, exercising appropriate judgement and meeting expectations of transparency; and
  - c) **value for money**: achieving economy, efficiency and effectiveness in the use of public resources.

### Exploring key terms (3): 'public service ethics'

- 1.18. Ethics relates to moral principles and rules of conduct which ascribe moral values to human actions within a social group or culture, with respect to the rightness or wrongness of actions and the goodness or badness of motives and outcomes. In public governance terms, ethical conduct and decision making are wider in scope than simply procedural correctness. The notion that actions and decisions should be based on what best serves the public's interests, as opposed to an official's personal interests, is fundamental to the concept of **public service ethics**.<sup>16</sup>
- 1.19. Public bodies are expected to adhere to an ethos based upon public sector values and standards, particularly in relation to openness and integrity in decision making, conduct and stewardship of money. Whilst these values and standards are not exclusive to the public sector, public service stakeholders have higher expectations of those whom they regard as being public servants, delivering public services or spending public money.

'These failings permeated the whole of the operations of the Partnership and suggest that those charged with responsibility for governance had little regard to recognised standards in public life or the need to achieve value for money from public funds.'

Source: **Plas Madoc Communities First**, March 2010

<sup>15</sup> The 'Wednesbury reasonableness test' was established in case law by the Court of Appeal in 1948. A decision is unreasonable (or irrational) if it is so unreasonable that no reasonable person acting reasonably could have made it. Good public governance requires more than the minimum standard of reasonableness established by the Wednesbury test.

<sup>16</sup> Institute of Local Government, **Understanding Public Ethics Law – Principles and California Law**, 2013

1.20. As well as serving the interests of a wider range of stakeholders than private bodies, public service bodies are required to deliver a wide range of political, economic and social goals and outcomes, many of which are qualitative and not directly measurable. In contrast, private organisations are driven by market forces and have a clearer profit motive, directly linked to the commercial interests of their funders and investors. Whilst private and public bodies both consider the interests of customers and staff as well as the organisation's reputation, private bodies primarily consider them in relation to their contribution to competitive advantage, profit generation and shareholder value, rather than to the public good.

### Exploring key terms (4): 'public servants'

- 1.21. Employment status can affect whether in addition to their employer's terms and conditions, staff are bound by the Civil Service code<sup>17</sup> or subject to a professional code of conduct. The employment and legal status of individuals involved in public services affects expectations of their conduct and also the potential consequences for them if their conduct falls short of the obligations placed upon them. The status of staff within the public sector who are performing similar functions can vary because they are employed by different types of public body. For example:
- a) administrative staff employed within the Welsh Government's Directorate for Health and Social Services are civil servants, whereas administrative staff employed by local health boards and trusts are not.
  - b) local health boards employ a range of health professionals. However, dentists, opticians, pharmacists and General Practitioners (GPs) provide services to the public under contractual agreements with the local health boards, but are not employed by them (although they are subject to external professional regulation).
  - c) where a local authority outsources a service, its employees will be transferred to a private provider. Although they may continue to perform the same function and role and aspects of their previous employment, terms and conditions may be protected; they will no longer be subject to the local authority's policies and procedures.

<sup>17</sup> Staff of the National Assembly (Assembly Commission) are bound by the Staff Code of Conduct; Welsh Government staff are bound by the Civil Service code.

- 1.22. Offences under the Bribery Act 2010 apply to anyone, whereas the common law offence of misconduct in public office applies only to holders of public office. There is no simple definition of who is or is not a ‘public officer;’ each case is assessed individually, taking into account the nature of the role, the duties carried out and the level of public trust involved. Public functions can be carried out by private employees and therefore a private employee may be a public officer for the purposes of the offence. The courts recognise the potential for unfairness if a public employee would be subject to a legal sanction whereas a private individual exercising the same function would not. Factors such as how the individual was appointed and whether they are paid or unpaid do not necessarily determine whether they are considered to be a public officer. Statutory and crown appointees as well as trustees do not have contracts of employment but are considered to be public officers. A factor that may point towards an individual being a ‘public officer’ is whether they have responsibility for ‘public funds’. However, there is no clear definition of what constitutes ‘public funds’.
- 1.23. Individuals appointed to be non-executive board members of public bodies are not usually employees of the body<sup>18</sup>. Conflicts of interest may arise for individuals who are appointed as board members of public bodies established as companies or as limited liability partnerships. This is because under company law, directors of all companies have a primary duty to act in the best interests of the company and must put the interests of the company before those of the sponsoring body. In most cases, the interests of both parties will align but situations can arise in which they do not. This issue may be particularly problematic where civil servants are also board members because their duty to the company may conflict with their responsibility to a minister under the Civil Service code.

‘RIFW Board members’ legal responsibilities were insufficiently aligned with the Welsh Government’s expectations of their collective accountability to Welsh Ministers.’

Source: **The Regeneration Investment Fund for Wales** (RIFW), July 2015

- 1.24. The position of ‘whistleblowers’ (people who raise issues of public concern about wrongdoing, risk or malpractice that they are aware of through their work) and the degree of legal protection afforded to them under the Public Interest Disclosure Act 1998, is the same, whether or not they are an employee and whether or not their employer is in the public or private sector. It is good practice for public sector bodies to have whistleblowing policies. Where public bodies are commissioning health and social care services, it is also good practice to extend their policy to encompass their contracted private and third sector service providers.

<sup>18</sup> The Wales Audit Office has a statutory board which includes two elected employee members.

1.25. However, well-publicised scandals brought to light by whistleblowers, such as the abuse of vulnerable residents at Winterbourne View<sup>19</sup> and the failings at Mid Staffordshire NHS Foundation Trust<sup>20</sup>, highlight issues about the treatment of whistleblowers. Without an appropriate organisational culture, people may be afraid to raise concerns and employers may fail to respond. Recent trends in employment practice towards zero-hours and fixed-term contracts may mean that due to the fear of victimisation, such staff could be less likely to raise issues of concern about working practices or inappropriate conduct by senior staff.

<sup>19</sup> Department of Health, **Transforming care: A national response to Winterbourne View Hospital**, December 2012

<sup>20</sup> **Report of the Mid Staffordshire NHS Foundation Trust Public Inquiry** [The Francis Report], February 2013

# Part 2

## 2. What are the key trends affecting the governance of indirectly provided, publicly funded services in Wales?

- 2.1. The growth of indirectly provided, publicly funded services in Wales is itself a response to wider political, economic, social and technological changes:
- a) the continuing climate of reductions in public spending is adding impetus to the already established trend towards exploring new models for delivering public services as a means of driving service improvements and reducing costs;
  - b) the dual pressures of rising demands and declining resources are encouraging policymakers to explore innovative ways of harnessing private and third sector expertise and capacity to meet these challenges; and
  - c) new information and communications technology provides opportunities for changing radically how services to the public or to government are accessed and how providers shape their organisations to deliver them, as well as raising ethical issues around information governance.
- 2.2. These changes interact to produce a dynamic and uncertain environment,<sup>21</sup> which drives innovation and decisions across Welsh public services to:
- a) establish new entities
  - b) procure services under contract
  - c) engage in partnerships
- 2.3. In Wales, since 1999 there has been less emphasis on competition, ‘purchaser/provider’ commissioning arrangements and privatisation than has been the case in England. Instead, the Welsh Government’s focus on partnership working and co-production has led to an increasingly diverse range of entities and individuals becoming involved in delivering Welsh public services as subsidiaries, agents, contractors or partners. The range of such organisations includes:
- a) arms-length agencies, including Welsh Government-owned companies such as Finance Wales PLC and its subsidiaries;
  - b) agents such as private sector fund and investment managers;
  - c) third sector organisations in receipt of grant funding;
  - d) not-for-profit organisations, such as leisure services trusts; and
  - e) private providers, such as care homes.

<sup>21</sup> The Auditor General set out the key financial challenges facing the Welsh public services in his report **A Picture of Public Services 2015**, published in December 2015.

- 2.4. The public services landscape in Wales is continuing to change, whilst at the same time public expectations are increasing in relation to service quality and also the standards of conduct exhibited by all organisations or individuals involved in public services and with public money. However, Wales is a small country and, in the complex landscape of public service provision, it is inevitable that actual or potential conflicts of interest will arise. Many individuals from the private sector participate in boards that commission and oversee publicly funded services; and because of their expertise, staff can move from holding policy or procurement responsibility within government to employment with private company suppliers.
- 2.5. Changes to policy and delivery system design increase the risk of that conflicts of interest may arise, for instance where both commissioner and provider functions are operated from within the same organisation. The Welsh Government has also emphasised local authorities' role in promoting social entrepreneurship, co-production and community initiatives, as exemplified in its 2015 draft Local Government (Wales) Bill. Such initiatives can result in local authorities entering into a variety of joint arrangements involving public, private and third sector individuals and entities. However conflicts, whether real or perceived, should always be managed effectively through measures that mitigate or eliminate them.

'The Welsh Government did not put in place effective compensating controls to mitigate a conflict of interest, and other governance around the decision to purchase was weak.'

Source: **The Welsh Government's acquisition and action to dispose of the former River Lodge Hotel, Llangollen**, June 2012

'Parties involved in executing the sale transaction had relationships with the buyer and the seller that gave rise to potential conflicts of interest.'

Source: **The Regeneration Investment Fund for Wales (RIFW)**, July 2015

'A conflict of interest was appropriately declared but this should have been handled more robustly by the Welsh Government.'

Source: **Establishment and oversight of the Wales Life Sciences Investment Fund**, February 2016

2.6. Well-managed risk taking is an important component in public service delivery systems. Overall, there is a pressing need for assurance that commercial approaches towards risk taking are being well managed when applied to using public resources and to delivering public services, regardless of the legal form of the entities involved or the status of their officers. Politicians, the media and the public all rightly expect that private entities and individuals involved in funding, procuring, managing, delivering and scrutinising publicly funded services will place the interests of service users and value for money in relation to public funds at the forefront. However, in some instances our audit work has indicated that the development of robust governance arrangements has failed to keep pace with innovation in delivery models and in working practices.

'We are concerned that high profile examples of poor grants management share common and recurring weaknesses. Key weaknesses we have identified have included a failure to adequately consider the viability, capacity and capability of recipients. In many instances, clarity of criteria and objectives has been lacking. We have also noted numerous instances of failure to adequately assess and mitigate risk. Weaknesses in ongoing monitoring also feature prominently in the list of recurring issues. Significantly, funders have failed to act on lessons learned when designing new schemes.'

Source: **Grants management in Wales**, November 2011

'The Welsh Government followed its procedures for approving and monitoring grant funding of the Project. However, the procedures at that time were less robust than those in place now and were unsuited to a project of this scale, complexity and risk. Although the Project achieved its main objectives, problems arose when the fish farm began operating which caused pollution and nuisance.'

Source: **Public funding of Penmon Fish Farm**, December 2013

'The project was always likely to fail because of flawed income assumptions and a lack of clarity over what the Centre was meant to offer, both of which were not adequately challenged by funders... Decisions to provide grant funding were based on highly flawed assumptions, particularly with regard to projected income levels... Funders did not identify and address all of the key risks and placed too much emphasis on the potential benefits of the project, and collaboration between funders was inadequate to support effective decision making.'

Source: **Public funding of the Cywain Centre, Bala**, April 2014

2.7. The Welsh Government seeks to learn lessons from individual governance failures, such as those highlighted in this paper, to ensure that they do not reoccur. However, the conceptual and practical difficulties involved in encouraging good governance in indirectly provided, publicly funded services indicate that a wider debate is timely.

# Part 3

## 3. How might implementation of the Well-being of Future Generations (Wales) Act influence the ethical governance of publicly funded services in Wales?

- 3.1. Recent legislation has placed increased requirements upon the conduct of Welsh public bodies, public servants and public services. The WFG Act provides a governance framework for decision making which aims to strengthen governance in Welsh public bodies, which must improve:  

‘The economic, social, environmental and cultural well-being of Wales by taking action in accordance with the sustainable development principle’. Acting in accordance with the sustainable development principle ‘means that the body must act in a manner which seeks to ensure that the needs of the present are met without compromising the ability of future generations to meet their own needs’.
- 3.2. The WFG Act requires the public bodies named within it to carry out sustainable development. The defining features which distinguish sustainable development from business as usual are:
  - a) an understanding of the long-term implications of decisions;
  - b) a recognition of environmental limits; and
  - c) an integrated approach to economic, social, environmental and cultural well-being.
- 3.3. The Act also places a well-being duty on those public bodies to set and publish well-being objectives in relation to their functions, designed to maximise their contribution to the seven national well-being goals. They are required to take all reasonable steps to meet those objectives, in accordance with the sustainable development principle. The sustainable development principle is defined through five ways of working. These are integration; collaboration; long-term thinking; involvement; and prevention.
- 3.4. The focus in decision making upon thinking long-term and considering prevention, whilst balancing resource pressures, will require a fundamental shift in the roles, skills and behaviours of many professionals. Public bodies must also involve service users and the wider public in taking an integrated and collaborative approach. All of these challenges pose ethical governance dilemmas, especially for those engaged in commissioning private sector providers to deliver public services.

Exhibit 2: the Welsh Government's objectives for the well-being of future generations

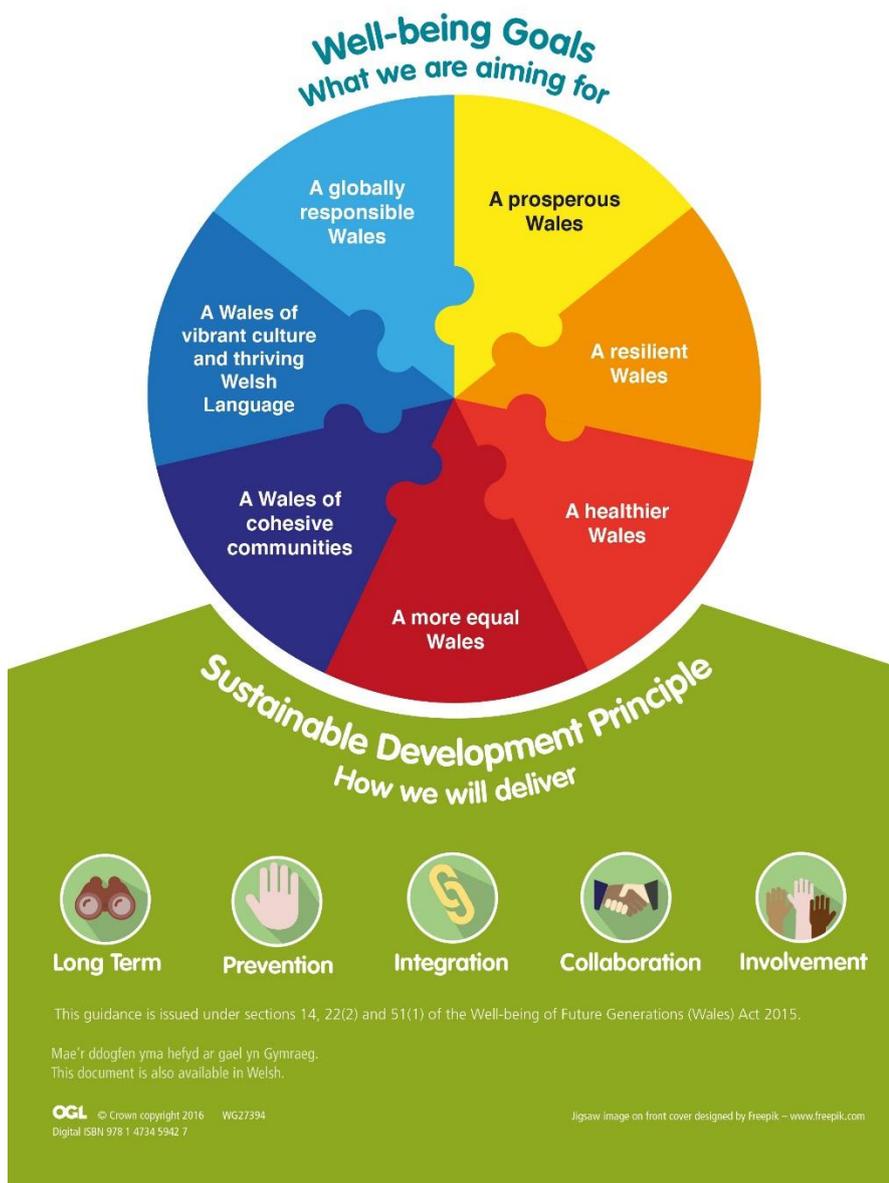


Exhibit source: Welsh Government, **Shared Purpose: Shared Future: Statutory guidance on the Well-being of Future Generations (Wales) Act 2015**

- 3.5. The WFG Act lists 44 public bodies delivering devolved services in Wales to which it applies, but the list is not comprehensive; for example, the Wales Ambulance Service Trust, Estyn and also the Public Services Ombudsman for Wales are not 'Welsh public bodies' for the purposes of the WFG Act. The four Welsh police forces are also not included, because policing is not a devolved function<sup>22</sup>.
- 3.6. The duties upon bodies named within the act do not extend explicitly to subsidiary bodies or to contractors. However, bodies named within the WFG Act will need to demonstrate that they are discharging their own statutory duties by acting in ways that are consistent with their well-being objectives. When providing funding, awarding grants or procuring services, a body named in the WFG Act may set remits, frame grant conditions or negotiate contract terms that are consistent with its well-being objectives and so have the effect of extending the WFG Act's scope beyond the public bodies defined within the WFG Act. However, it is unclear how implementation of the WFG Act will influence the ethical governance of:
- a) public bodies in Wales not named in the act;
  - b) subsidiaries of Welsh public bodies; and
  - c) private or third sector providers of publicly funded services.
- 3.7. An inherent tension exists between the WFG Act's requirement for the bodies named within it to take a longer-term view and annual funding, budgeting and accounting cycles in operation across Welsh public bodies. Implementing the WFG Act's requirements is likely to increase the internal and external governance focus upon and scrutiny of strategic plans and medium-term financial plans, as is already happening in NHS Wales. In order to meet their responsibilities under the WFG Act, many Welsh public bodies are pressing the Welsh Government to give them greater certainty in relation to future funding, as well as financial flexibilities similar to those of NHS bodies<sup>23</sup>. Or at least, greater clarity in relation to funders' priorities and the range within which their funding decisions may lie.

<sup>22</sup> Public service boards established under the WFG Act are required to invite the chief constable and police and crime commissioner to participate in the partnership for the local authority area covered by the board.

<sup>23</sup> Financial duties differ between the seven Welsh local health boards and the three Welsh NHS trusts. Local health boards must not exceed their spending limits over a three-year rolling period. Failure leads to a qualified external audit opinion. Trusts have a duty to break-even over a rolling three-year period but failure to do so does not lead to audit qualification. The financial duties for NHS bodies differ from those of most Welsh public bodies, which are required to break-even each year.

'NRW informed us it finds annual budget allocations from the Welsh Government restrictive but manages the impact through its financial planning and modelling. However, there is a risk that budget cuts require an even greater prioritisation of work with difficult decisions to be made, particularly given uncertainty over any additional funding for new statutory responsibilities. NRW considers that the expected level of budget cuts will require fundamental changes to the purpose and structure of NRW.'

Source: **The development of Natural Resources Wales (NRW)**, February 2016

- 3.8. Rising citizen expectations of Welsh public services, reflected in the WFG Act's seven well-being goals, require fundamental changes in all Welsh public bodies' processes, performance management systems and culture. The existing emphasis upon historical information based upon centrally driven performance indicators, budget administration and external financial reporting requirements will no longer be sufficient. Instead, there is a clear need for qualitative improvements in forward-looking performance and financial information that supports business cases, options appraisal, strategic planning and decision making. In essence, modelling the impacts of changes in activities, costs, incomes and demands, together with robust outcome monitoring, will be key to achieving each body's well-being objectives.
- 3.9. For private sector organisations engaged in commercial activity, the quality of management information is generally an internal matter, although business analysts and private investors take a keen interest. However, when private and third sector organisations are involved in providing public services, then sponsor access, quality assurance and the public transparency<sup>24</sup> of management information should be stipulated in:
  - a) procurement contracts
  - b) partnership agreements
  - c) grant conditions
- 3.10. Accomplishing these changes is likely to require public bodies to acquire or develop the necessary skills, technology and capacity to gather, analyse and use the information. The growth of digital data technology presents many opportunities, but also raises information governance issues in areas such as the ethics of data capture, sharing, retention, use, transparency, access and security.

<sup>24</sup> The National Audit Office urges adoption of 'open-book accounting' practices which provide transparency of payments, performance and profits in relation to outsourced services, as a fundamental condition of doing business with the public sector. [National Audit Office, **Open-book accounting and supply-chain assurance**, June 2015].

'As an audit body, we are particularly concerned to encourage development of the finance profession in Wales. Some of our recent reports have commented on the lack of financial capacity and capability in many of the bodies we audit. The finance function has traditionally been about budget setting, control and compliance. In some cases, the finance function is seen as a barrier to innovation and change where it is averse to risk. In the future, finance professionals will have a greater role as a strategic partner to services, offering insight for example to support business plans for new ways of working. Finance and other professionals will need to take a long-term view of the costs and benefits of changes in the round.'

Source: **A Picture of Public Services 2015**, December 2015

- 3.11. There are also governance challenges in relation to sponsor, executive and non-executive oversight and scrutiny, as well as for regulation and audit. The WFG Act created the office of the Future Generations Commissioner (a corporation sole at arms-length from government). The commissioner's role is to support the 44 public bodies named in the act, including the Welsh Government, to work towards achieving the Welsh Government's well-being goals and to monitor and report on their progress. The WFG Act also set up new public service boards<sup>25</sup> to undertake a baseline assessment of local well-being, produce area well-being plans and to report on progress. In addition, the WFG Act placed a duty upon the Auditor General to provide a report to the National Assembly during each assembly election cycle, on the extent to which the bodies named in the WFG Act have applied the sustainable development principle in setting and meeting well-being objectives.
- 3.12. In order to mitigate the risk of increasing the quantity of regulation and assessment of public bodies, as well as the risk of conflicting or contradictory conclusions and recommendations, the Auditor General and the Future Generations Commissioner have agreed to co-operate in relation to their respective responsibilities under the WFG Act. This co-operation provides an opportunity to develop a more streamlined, seamless and coherent assessment of public bodies whilst also ensuring that everyone involved in these functions has the necessary skills and interpretive insight to critically appraise information placed before them and to judge how much reliance to place upon it.
- 3.13. Implementing the WFG Act will clearly impact upon the governance of the bodies named within it and has implications for audit and regulation. However, at present, the implications are less clear for public bodies not named within it, including subsidiaries, and also for private and third sector bodies who provide public services.

<sup>25</sup> Public service boards established under the WFG Act in each local authority area in Wales are statutory partnerships but are not entities in their own right.

# Part 4

## 4. How can greater clarity be achieved in relation to the attitudes and behaviours expected of individuals and entities involved in Welsh public services?

- 4.1. The two traditional approaches to strengthening governance can be categorised as being primarily either principles-based or rules-based. These differing approaches are not mutually exclusive and may work in tandem; 'rules' can be used to specify when and how 'principles' should be applied. However, neither approach alone is appropriate in all circumstances because:
- a) principles set out broad expectations whilst providing flexibility in practice. However, it may be unclear whether they should apply, how they should be applied and how any tensions between different principles should be resolved.
  - b) rules are specific and prescriptive. Writing rules into regulations and agreements may be more easily enforceable than principles but, whilst rules leave less room for interpretation, they invariably give rise to some situations that are not explicitly covered.

### Principles-based approaches to strengthening governance

- 4.2. Across the UK public sector, the principles-based approach to governance is encapsulated within the Nolan Principles<sup>26</sup> of:
- a) selflessness
  - b) integrity
  - c) objectivity
  - d) accountability
  - e) openness
  - f) honesty
  - g) leadership

<sup>26</sup> The Nolan Principles were set out in 2013 by the Committee on Standards in Public Life, chaired by Lord Nolan, in its **Fourteenth Report**. They are listed in full in Appendix 1.

4.3. Within Wales, Academi Wales has emphasised the importance of a public service ethos:

‘...whilst diversity and new ways of working are embraced and encouraged, common values and standards are understood and applied across the public service in Wales.’

Although Academi Wales recognises that:

‘There is no hard and fast definition of the Welsh public service...’

The academi endorses:

‘...the Welsh Public Service Values, the Nolan Principles, and Citizen-Centred Governance Principles for Wales.’<sup>27</sup>

And it proposes that these:

‘...apply to any organisation that delivers public services to the people of Wales and/or utilises Welsh public funding directly or indirectly.’<sup>28</sup>

4.4. Importantly, the Westminster Parliament’s Committee on Standards in Public Life has stated that there should be a wider application of the Nolan Principles of conduct in public life (hitherto applied to all appointed or elected public servants) and has invited debate on how the principles should be extended to all those involved in publicly funded services<sup>29</sup>. The chair of that committee, Lord Bew, has also commented that:

‘...any organisation providing any public service should ensure that such [ethical] standards form part of its culture and behaviour and are demonstrated in practice from start to finish... It is the responsibility of the Welsh Government to ensure that this is achieved, regardless of who is providing the service.’

4.5. **Managing Welsh Public Money** (MWPM) is the Welsh Government’s primary guidance<sup>30</sup> on the proper handling of public funds. It aims to provide a reference guide to be applied by the Welsh Government and by the bodies it sponsors on how to handle public funds with probity and in the public interest. MWPM stresses the application of the Citizen Centred Governance Principles for Wales to public service organisations funded by the Welsh Government and the Nolan Principles to individuals working for the public service in Wales.

<sup>27</sup> These principles are set out in Appendix 2.

<sup>28</sup> Academi Wales, **The Good Governance Guide: Doing it right, doing it better**, Draft, January 2016

<sup>29</sup> The Auditor General’s February 2016 report on the Welsh Life Sciences Investment Fund cites both the January 2013 and June 2014 reports of the Committee on Standards in Public Life, which has identified this area as requiring further careful consideration.

<sup>30</sup> Updated and re-published in February 2016.

- 4.6. The Citizen Centred Governance Principles for Wales are aligned with the requirements of the WFG Act. The WFG Act adopts an approach based upon the sustainability principle<sup>31</sup> rather than a prescriptive approach, which provides opportunities for Welsh public bodies (as defined in the act) to ensure that their response is proportionate, so that they can fulfil the WFG Act's requirements in ways which are tailored to the scale of the organisations' activities and expenditure.
- 4.7. In addition to the Nolan Principles and the Citizen Centred Principles for Wales, other principles are relevant to Welsh public bodies. These include NHS in Wales Core Principles and Values and also Procurement Principles<sup>32</sup>. The **Wales Procurement Policy Statement** sets out ten principles for procurement for all Welsh 'public sector' organisations. This policy adopts the Sustainable Procurement Task Force (in **Procuring the Future**, 2006) definition of procurement:
- 'the process whereby organisations meet their needs for goods, services, works and utilities in a way that achieves value for money on a whole life basis in terms of generating benefits not only to the organisation, but also to society and the economy, whilst minimising damage to the environment.'
- 4.8. The various sets of principles are not fully aligned but neither are they incompatible. It is left to bodies themselves to draw the various principles together from diverse sources. For example, the **Wales Procurement Policy Statement** (which contains the procurement principles) states that the Welsh public sector will promote fair payment terms; a commitment which is compatible with the public sector payment policy target and with the WFG Act. However, the public sector payment policy target itself<sup>33</sup>, is not explicit within the policy statement.
- 4.9. The consistent application of principles is problematic, because there is no consensus about the extent to which the various principles can, or should be, applied in practice:
- a) there is a plethora of differing sets of principles, many of which aim to apply universally to the public sector, public services and/or public money (see **Appendices 1 and 2**);
  - b) terms such as 'Welsh public funding' and 'public services' are not defined consistently or clearly (see **Part 1**); and

<sup>31</sup> See also Appendix 2.

<sup>32</sup> Contained within the **Wales Procurement Policy Statement**, published by the Welsh Government in 2012, updated and republished in 2015. See Appendix 2.

<sup>33</sup> The standard terms for UK government contracts is for payment within 30 days. Whenever possible, central government bodies will pay within 10 days.

- c) the status of different sets of principles is variable and it is unclear which principles have legal status through either statute<sup>34</sup> or case law<sup>35</sup>, and which are merely advisory.

4.10. There may be conflicts between different principles and sets of principles.

For example, circumstances may arise in which there is a tension between value for money for the organisation and potential wider social benefits from sourcing within the local economy. In such cases, decision-makers will need to be able to demonstrate that they have taken reasonable steps to apply principles and have taken all relevant matters into account when reaching their decision, otherwise they may be exposed to the risk of successful judicial review.

## Rules-based approaches to strengthening governance

- 4.11. Rules may be legislative, administrative, contractual or a combination of these. They can relate to how a body is established, how it operates and how individuals within it are held accountable for its performance and for their actions. The Companies Act 2006 places a statutory responsibility on the directors to maintain a reputation for high standards of business conduct, to avoid conflicts of interest, to declare interest in a transaction or arrangement and not to accept benefits from third parties for being a director, or for doing, or not doing anything as a director. The board, its directors, employees and those funded by the company must not act or take decisions in order to gain financial or other material benefits for themselves, their family or their friends. They must declare any interests and relationships. Whilst these responsibilities are applicable to companies in government and are analogous to the Nolan Principles, the prime responsibility of directors is to the entity, not to the wider public (see also [paragraph 1.23](#)).
- 4.12. At present, the UK Government is tidying up arms-length bodies, classifying them and producing rules for establishing new ones. In Scotland, the Scottish Government maintains a single register of all devolved public bodies, including details of their funding, staffing and chief executives' pay. In Wales, the Welsh Government is cataloguing public bodies, producing governance guidance and ethical standards for subsidiary companies and publishing MWPM along with principles for the public sector.

<sup>34</sup> For example, the WFG Act.

<sup>35</sup> For example, the principle of reasonableness established in case law by the 'Wednesbury reasonableness test' (see also [paragraph 1.17](#)).

4.13. Business cases under which the Welsh Government seeks to establish any new public bodies in Wales are reviewed by the Welsh Government's Corporate Governance Unit which provides financial and legal advice. The Corporate Governance Unit's review includes checking the rationale for setting up a new body. However, at present there is no clear framework within which new public bodies in Wales (whether by central or local government) must be established. Establishing new bodies within a framework of guidelines that are departed from only by exception and with clear justification, would allow for flexibility whilst increasing clarity, consistency and predictability.

'In establishing RIFW's governance arrangements, the Welsh Government failed to make explicit the oversight mechanism for RIFW as an arm's-length body.'

Source: **The Regeneration Investment Fund for Wales** (RIFW), July 2015

'In establishing RIFW's governance arrangements, the Welsh Government failed to make explicit the oversight mechanism for RIFW as an arm's-length body.'

Source: **The Regeneration Investment Fund for Wales** (RIFW), July 2015

'Plas Madoc Communities First [PMCF] is a company limited by guarantee and a registered charity... The audit investigation found a fundamental lack of financial control and governance at PMCF.'

Source: **Plas Madoc Communities First**, March 2010

4.14. In its 2013 publication, **Standards Matter**, the Committee for Standards in Public Life stated:

'Public servants designing and commissioning services should, in a consistent and proportionate way, address ethical issues throughout the procurement process. Contractors and others should acknowledge the particular responsibilities they bear when delivering public services, paid for by public money, to individuals who may not have the choice of going elsewhere. .... Unless the principles are clearly translated into contracts and clear guidance, it is unlikely that private contractors in particular will believe that they are unambiguously applicable to them (given the likelihood of conflicts between the motives of private profit and public service), or spend time deducing from the principles how they are supposed to behave. There is therefore a responsibility on public office-holders to specify particular and proportionate ethical requirements in the contracts they let on behalf of the public sector ..... unless the public sector does specify ethical requirements in its contracts it is unlikely that the market will operate to drive up ethical as well as quality standards and value for money.'

- 4.15. Ultimately the only way of ensuring that organisations providing outsourced public services operate to the standards of conduct expected of public bodies is by introducing additional contractual requirements within procurement and commissioning processes. Public bodies can also write the requirement for private sector bodies to follow public sector practices into grant conditions and loan agreements.
- 4.16. The Welsh Government's standard grant conditions require applicants to comply with legal requirements and regulations, and also require all necessary permits and consents to be in place. However, Welsh Government grant conditions do not routinely include any general requirement for the grant recipient to comply with standards of conduct in business. If the Welsh Government was able to develop an enforceable condition that covered such requirements, its inclusion would help to safeguard public funds used for grant-funded projects. It would also mitigate potential risks to the Welsh Government's reputation, through association with recipients which did not meet the requirements of such a condition<sup>36</sup>.

'The Welsh Government identified potential risks when it approved grant funding for the Project, but did not put in place grant conditions that would have helped mitigate the risks.'

Source: **Public funding of Penmon Fish Farm**, December 2013

All funders had recognised, to varying degrees, the unsupported and unrealistic assumptions that underpinned the business case for the Centre. However, they approved grant funding without putting in place fully effective measures to mitigate and manage the risks to the project they had identified... Grant conditions, the main mechanism for managing the risks identified, were not always comprehensive or realistic.'

Source: **Public funding of the Cywain Centre, Bala**, April 2014

<sup>36</sup> Auditor General for Wales, **Public Funding of Penmon Fish Farm**, December 2013

- 4.17. There is no particular obstacle to including contractual requirements for standards of conduct. The real difficulty lies in how to articulate public sector values as contractual requirements in a way which is unambiguous, measurable, capable of being monitored and enforceable. This is an area in which significant development is needed. The Westminster Parliament's Committee for Standards in Public Life outlined a number of procurement/contractual mechanisms which purchasers/commissioners should consider in relation to:
- a) contract design/tendering
  - b) contractual requirements<sup>37</sup>
- 4.18. Model contract terms and conditions in respect of governance and accountability arrangements and anti-bribery and fraud and corruption have already been developed and are included in the UK Government's Legal Service Model Contract terms. The National Audit Office has recommended that to ensure transparency in relation to contracted-out services, a requirement for 'open-book accounting' should be written in to all contracts<sup>38</sup>. Companies, social enterprises and charities wishing to bid for public service contracts above a nationally agreed contract size, value threshold and political sensitivity should accept this condition or simply not bid. However, it is important that transparency should not be a burden or a barrier to small organisations or result in disproportionate costs.

<sup>37</sup> These include The Merlin Standard which was designed to recognise and promote sustainable excellence within supply chains and provide guidance to those seeking to achieve it. It is built upon four fundamental and integrated principles: supply chain design, commitment, conduct and review. These principles were designed to examine key areas of the relationship between a prime contractor and its supply chain partners. The Merlin Standard was originally developed by the DWP. A large number of suppliers are already Merlin accredited and all accredited main contractors are required to ensure they and all subcontractors comply with the DWP code of conduct. [Committee for Standards in Public Life, **Ethical Standards for Providers of Public Services** – guidance, December 2015]

<sup>38</sup> 'Open-book accounting' provides the public with the same transparency of payments, performance and profits for outsourced services as would be the case if the services were provided 'in-house' by the public sector. [National Audit Office, **Open-book accounting and supply-chain assurance**, June 2015]

- 4.19. There are also a number of non-contractual mechanisms which the public sector can use to encourage providers of public services to comply with high standards of conduct. These include:
- a) ethical codes for providers
  - b) standards for, and assessments of, supply chains
  - c) 'mystery shopper' arrangements
  - d) analysis of user complaints
  - e) effective commissioner-provider relationships
  - f) process of corporate renewal and development of 'good corporate citizen'
  - g) open publication of contract availability
- 4.20. Regardless of whether governance expectations that reflect the public sector ethos are expressed as principles or as rules, mechanisms are necessary to embed them in all commissioners and providers of public services; to provide compliance standards and monitoring measures. These must not be so burdensome as to intrude unnecessarily, constrain innovation, drive down efficiency or to undermine sustainability. However, they must constitute a framework that provides clarity whilst embracing diversity and which supports accountability, incentivises improvement, and mitigates inherent risk.

## Encouraging the right behaviours

- 4.21. Any governance system, whether based on principles or rules, will fail to be effective if those charged with governance are not familiar with what is expected of them or fail to give the area sufficient attention. Training, awareness and clear, readily available guidance are key in supporting all those who deliver public services to do so in a manner which enables them to achieve their objectives and to live up to the values expected of them.

# Appendix 1

## The Nolan Principles

In its **Fourteenth Report**, the Committee on Standards in Public Life (2013) emphasised that standards of behaviour matter and are particularly important where public money is being spent on public services or public functions. The principles are universal:

- **selflessness:** holders of public office should act solely in terms of the public interest.
- **integrity:** holders of public office must avoid placing themselves under any obligation to people or organisations that might try inappropriately to influence them in their work. They should not act or take decisions in order to gain financial or other material benefits for themselves, their family, or their friends. They must declare and resolve any interests and relationships.
- **objectivity:** holders of public office must act and take decisions impartially, fairly and on merit, using the best evidence and without discrimination or bias.
- **accountability:** holders of public office are accountable to the public for their decisions and actions and must submit themselves to the scrutiny necessary to ensure this.
- **openness:** holders of public office should act and take decisions in an open and transparent manner. Information should not be withheld from the public unless there are clear and lawful reasons for so doing.
- **honesty:** holders of public office should be truthful.
- **leadership:** holders of public office should exhibit these principles in their own behaviour. They should actively promote and robustly support the principles and be willing to challenge poor behaviour wherever it occurs.

# Appendix 2

## Welsh public service values and behaviours

### Public service values and behaviours for Wales

The Welsh Government has set out an ambitious agenda to unify public service endeavour across Wales with a common set of values, bringing together the responsibilities of the Future Generations (Wales) Act 2015:

- behaving with integrity, demonstrating strong commitment to ethical values, and respecting the rule of law;
- ensuring openness and comprehensive stakeholder engagement;
- defining outcomes in terms of sustainable economic, social and environmental benefits;
- determining the interventions necessary to optimise the achievement of the intended outcomes;
- developing the entity's capacity, including the capability of its leadership and the individuals within it;
- managing risks and performance through robust internal control and strong public financial management; and
- implementing good practices in transparency, reporting, and audit to deliver effective accountability.

### Procurement principles for Wales

The **Wales Procurement Policy Statement**, published by the Welsh Government in 2015, sets out ten principles for procurement for all Welsh 'public sector' organisations:

- **strategic:** procurement should be recognised and managed as a strategic corporate function that organises and understands expenditure; influencing early planning and service design and involved in decision making to support delivery of overarching objectives.
- **professionally resourced:** procurement expenditure should be subject to an appropriate level of professional involvement and influence, adopting the initial benchmark of a minimum of one procurement professional per £10m of expenditure across the wider public sector.
- **economic, social and environmental impact:** Value for Money should be considered as the optimum combination of whole-of-life costs in terms of not only generating efficiency savings and good quality outcomes for the organisation, but also benefit to society, the economy, and the environment, both now and in the future.

- **community benefits:** delivery of social, economic and environmental benefit through effective application of Community Benefits policy must be an integral consideration in procurement.
- **open, accessible competition:** public bodies should adopt risk based, proportionate approaches to procurement to ensure that contract opportunities are open to all and smaller, local suppliers are not precluded from winning contracts individually, as consortia, or through roles within the supply chain.
- **simplified standard processes:** procurement processes should be open and transparent and based on standard approaches and use of common systems that appropriately minimise complexity, cost, timescales and requirements for suppliers.
- **collaboration:** areas of common expenditure should be addressed collectively using standardised approaches and specifications managed by the National Procurement Service (NPS) to reduce duplication, to get the best response from the market, to embed the principles of this Policy Statement for the benefit of Wales; and to share resources and expertise.
- **supplier engagement and innovation:** dialogue with suppliers should be improved to help get the best response from the market place, to inform and educate suppliers, and to deliver optimum value for money.
- **policy development and implementation:** deployment of policy which supports the achievement of the seven well-being goals for Wales as set out in the Well-being of Future Generations (Wales) Act (2015).
- **measurement and impact:** in accordance with good management practice, procurement performance and outcomes should be monitored to support continuous improvement, and examples of good and poor practice openly shared.

## Citizen Centred Governance Principles for Wales

- putting the citizen first: putting the citizen at the heart of everything and focusing on their needs and experiences; making the organisation's purpose the delivery of a high quality service.
- knowing who does what and why: making sure that everyone involved in the delivery chain understands each other's roles and responsibilities and how together they can deliver the best possible outcomes.
- engaging with others: working in constructive partnerships to deliver the best outcome for the citizen.
- living public sector values: being a value-driven organisation, rooted in Nolan Principles and Welsh Public service values. High standards of public life and behaviour, including openness, customer service standards, diversity and engaged leadership.
- fostering innovative delivery: being creative and innovative in the delivery of public services – working from evidence, and taking managed risks to achieve better outcomes.

- being a learning organisation: always learning and always improving service delivery.
- achieving value for money: looking after taxpayers' resources properly, and using them carefully to deliver high quality, efficient services.

## The NHS in Wales – principles and core values

The NHS **Governance e-Manual** identifies a number of core values for the NHS in Wales, namely:

- putting quality and safety above all else
- integrating improvement into everyday working
- focusing on prevention, health improvement and inequality
- working in partnership
- investing in staff

These core values are designed to support good governance and the achievement of high standards of care. Alongside these, specific codes of conduct for board members and NHS managers have been developed which incorporate the Seven Principles of Public Life (the Nolan Principles). In addition, there are policies on specific areas, including whistleblowing and compromise agreements described within Openness and Business Conduct.

## The NHS in Wales – standards for services

**Doing Well, Doing Better – Standards for Health Services in Wales** contains 26 standards that set out the requirements of all services in all settings in the NHS in Wales. These standards were introduced in 2010, replacing the previous ones launched in 2005.

The standards framework is underpinned by supporting guidance for individual standards and how to guides which give practical advice on how to implement them. A Governance and Accountability module provides NHS boards with a framework to monitor performance against the standards. This largely takes the form of self-assessment against maturity matrix descriptions.

At the time of preparing this briefing, the Welsh Government was undertaking a review of the Standards for Health Services in Wales.

The Standards for Health Services in Wales sit alongside a number of other mechanisms that set out what is required in delivering services to patients. These include a suite of delivery plans for specific conditions such as heart disease, stroke, diabetes, respiratory health and eye health amongst others. These plans typically set out the key actions that need to be taken to improve healthcare outcomes for patients. Many of these delivery plans have replaced national service frameworks that had previously been developed for these conditions.

## Governance in the NHS in Wales

Other key mechanisms for setting out patient-care requirements comprise:

- the range of professional standards and regulations that apply to specific health professions and services.
- **Fundamentals of Care** guidance which was produced by the Welsh Government in 2003 and contains a set of indicators that cover fundamental aspects of quality that are important to anyone receiving health or social care.
- the National Institute for Health and Care Excellence standards, guidance and advice on a wide range of health and care service areas in Wales.
- the Quality and Outcomes Framework for GPs is a voluntary framework that aims to reward GPs for providing good practice. Practices are awarded points for providing evidence of good practice covering four domain of general practice: clinical, organisational, patient experience and additional services.

Notes:

- NHS Wales, [Governance e-Manual: Codes of Conduct](#)
- NHS Wales, [Governance e-Manual: Openness and Business Conduct](#)
- Welsh Government, [Doing Well, Doing Better: Standards for Health Services in Wales](#), 1 April 2010

# Appendix 3

## Selected further reading

Auditor General for Wales' reports:

- **Plas Madoc Communities First**, March 2010
- **Grants management in Wales**, November 2011
- **The Welsh Government's acquisition and action to dispose of the former River Lodge Hotel, Llangollen**, June 2012
- **The Welsh Government's relationship with the All Wales Ethnic Minority Association (AWEMA)**, October 2012
- **Public funding of Penmon Fish Farm**, December 2013
- **Public funding of the Cywain Centre, Bala**, April 2014
- **Governance in the NHS in Wales**, Memorandum for the Public Accounts Committee, April 2015
- **The Regeneration Investment Fund for Wales (RIFW)**, July 2015
- **A Picture of Public Services 2015**, December 2015
- **Establishment and oversight of the Wales Life Sciences Investment Fund**, February 2016
- **The development of Natural Resources Wales (NRW)**, February 2016

National Audit Office reports:

- **Open-book Accounting and Supply-chain Assurance**, June 2015
- **Department's oversight of arm's length bodies: a comparative study**, July 2016

National Assembly Public Accounts Committee report:

- National Assembly for Wales Public Accounts Committee, **Senior Management Pay**, November 2014

Publications produced or commissioned by the Welsh Government:

- The Welsh Government, **Wales Procurement Policy Statement**, 2015
- The Commission on Public Service Governance and Delivery [The Williams Commission], **Full Report**, January 2014
- The Welsh Government, **Shared Purpose: Shared Future: Statutory guidance on the Well-being of Future Generations (Wales) Act 2015**
- The Welsh Government, **Managing Welsh Public Money (MWPM)**, updated and re-published February 2016

Other relevant material:

- Department of Health, **Transforming care: A national response to Winterbourne View Hospital**, December 2012
- **Report of the Mid Staffordshire NHS Foundation Trust Public Inquiry** [The Francis Report], February 2013
- CIPFA/IFAC, **International Framework: Good Governance in the Public Sector**, 2014
- The Committee for Standards in Public Life, **Ethical Standards for Providers of Public Services – guidance**, December 2015
- Academi Wales, **The Good Governance Guide: Doing it right, doing it better**, Draft, January 2016



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