



National Audit Office

National Audit Office

Our Strategy 2012-13 to 2014-15

Our vision is to help the nation spend wisely.

We apply the unique perspective of public audit to help Parliament and government drive lasting improvement in public services.

The National Audit Office scrutinises public spending on behalf of Parliament. The Comptroller and Auditor General, Amyas Morse, is an Officer of the House of Commons. He is the head of the NAO, which employs some 880 staff. He and the NAO are totally independent of government. He certifies the accounts of all government departments and a wide range of other public sector bodies; and he has statutory authority to report to Parliament on the economy, efficiency and effectiveness with which departments and other bodies have used their resources. Our work led to savings and other efficiency gains worth more than £1 billion in 2010-11.

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National Audit Office

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Our Strategy 2012-13 to 2014-15

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Foreword

The NAO strategy is driven by the key issues and major changes faced by the public sector. These create the context in which we assess whether government uses resources efficiently and effectively, delivers value for money and reports comprehensively to Parliament. These issues also inform us how to target our work in areas where it will be most effective, both in evaluating efficiency and in pointing to best practice and opportunities for improvement, particularly in delivering public value and improving financial reporting.

The NAO is becoming progressively more sophisticated in building and using its skills and knowledge. But we have much further to go in understanding government's complex and evolving challenges and the resulting changes.

Some of these changes involve us directly, including extending our responsibilities as a result of the new audit arrangements proposed for local government. The establishment of ministerial boards in central government, and the increase in centrally-funded devolved structures in education and health, have also triggered discussion about accountability that is relevant to our work. In each case, we work closely with government and Parliament, and with the Committee of Public Accounts in particular, to inform debate, always subject to our primary role of helping Parliament to hold the executive to account.

Over the last two years, the NAO has shown that it can be more cost-efficient and achieve more impact, while building strong, professional relationships with Parliament and the wider public sector. The dedication, skill and public service commitment of NAO staff has been very evident in making this happen.

Looking ahead, the NAO will match the development of complex, fast-moving public sector issues in its interventions. To do so, it will ensure that the cultural change already under way is carried through in maximising the development of our people as professionals, combining disciplines and skills in a way which delivers the full potential benefit to Parliament and to the public sector.

Amyas C E Morse
Comptroller and Auditor General

Professor Sir Andrew Likierman
Chairman

Part One

Our strategy

Summary

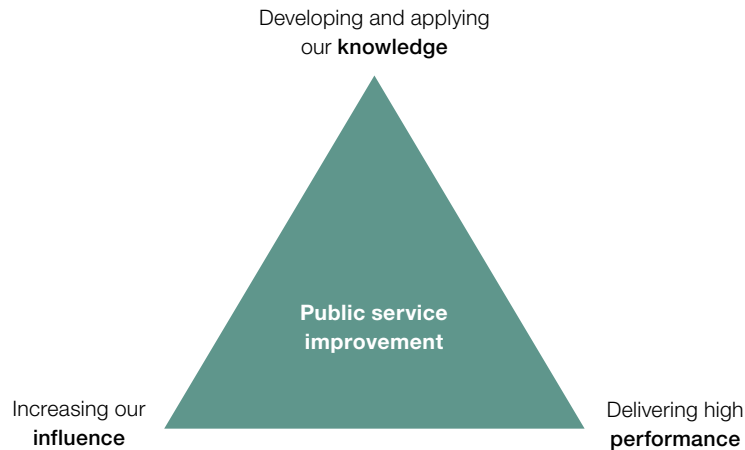
1.1 *In October 2009, we published a three-year strategy that focused on developing the ways in which public audit can help government to improve public services. We set ourselves challenging objectives aimed at creating a high-performance organisation that would help Parliament to hold government to account for its use of public money (see **Figure 1** overleaf). Two years into our strategy, those goals are even more relevant. We remain committed to delivering our strategy to ensure that public money is used wisely and well.*

Our aim and objectives

1.2 The NAO's aim is, through some 460 financial audits, 60 value-for-money reports and other work, to apply the unique perspective of public audit to help Parliament and government drive lasting improvement in public services. To achieve this aim the NAO must:

- be a high performing organisation that consistently demonstrates leading edge competencies in its core disciplines;
- develop and apply its expert knowledge to provide an independent and objective assessment of government performance; and
- use its knowledge to influence departments to drive improvement across public services.

Figure 1
NAO objectives 2010-11 to 2014-15



1.3 We have made progress in achieving our objectives. We have broadened the range of our products and increased the speed of their delivery. MPs and government departments tell us in independent surveys that they value our work.¹ In addition, our financial audit work is reviewed annually by the Audit Inspection Unit to ensure we maintain standards of audit quality. We have achieved this progress while remaining on track to reduce our own costs by 7.3 per cent in 2011-12 and by a total of 15 per cent in the three years to 2013-14.

1.4 We are committed to our strategy. Our operating environment is evolving, but our aim and objectives remain relevant. We have deep expertise in financial management, in the use of information to inform decisions, and in ways to implement projects cost-effectively. All these are areas of critical importance to Parliament and to government. We are determined to use this knowledge to add maximum value to the resources allocated to us, becoming ever more efficient and effective in our work.

1.5 This document summarises how we will update our existing strategy to reflect recent changes. Part Two summarises developments in public services, and Part Three highlights the impact of our strategy so far. In Part Four, we outline how we will continue to develop our capability over the next two years and Part Five details the resources we will need to deliver our work while continuing to reduce our own costs. Finally, in Part Six we set out how we will measure our performance.

¹ Moderated feedback from NAO clients conducted independently by Grant Thornton, 2011 and Ipsos MORI survey of MPs 2011.

Part Two

Developments in public services

Summary

2.1 *There have been significant changes across the public sector over the last two years, adding major programmes of cost reduction and structural reform to the existing demands of maintaining public services. Implementing these changes brings potential risks to value for money and to accountability, as well as opportunities to strengthen Parliamentary scrutiny, including through greater transparency. The NAO has expertise and insight that can help public sector bodies to overcome the many challenges they face.*

A demanding policy landscape

2.2 The political and economic changes of the last two years have had a significant impact on the bodies we audit. The coalition government has an ambitious programme of public sector reform to deliver with reduced resources. Government departments are now implementing wide-ranging cost reduction programmes and, in some cases, significant structural reform.

2.3 In health, education, policing and local government, the planning and provision of services is becoming more local, involving new forms of partnership working. Democratic accountability to Parliament for national funding is being supplemented by more visible local accountability for the use of public money, with pilots exploring how 'community budgets' might enable bodies to pool their resources in pursuing joint outcomes. Greater transparency is intended to help taxpayers and service users to see more clearly how their money is being spent.

2.4 These changes are likely to result in a more diverse public sector, with greater voluntary and private sector involvement in public services, and the provision of services differing more markedly from area to area. Further innovation may in time lead to yet more models of public service delivery.

2.5 The reforms may create opportunities for the public sector to become more accountable to local people and to operate with improved value for money. But the speed and scale of change may also bring risks including from funding uncertainty, more complex delivery models, and new scrutiny and accountability arrangements. These risks to value for money will need to be identified and addressed as policy changes are implemented.

A challenging fiscal landscape

2.6 The 2010 Comprehensive Spending Review described the intense pressures on public finances. Bodies across the public sector are now implementing plans to save money by cutting waste, reducing staff headcount, and re-designing services. The level of reductions involved is, in some cases, unprecedented. No part of the public sector is immune from the immediate challenge of delivering more for less.

2.7 These fiscal challenges will remain for a number of years. It will be important for public bodies to demonstrate that they can reduce expenditure while continuing to drive improvement in public services.

A changing audit landscape

2.8 The last two years have seen significant changes to financial reporting in central government. In 2010-11, government departments, their agencies and most arms'-length bodies prepared their accounts under International Financial Reporting Standards for the first time. Progress was also made in delivering the Whole of Government Accounts, with the Government producing a single set of comprehensive group accounts for the entire public sector.

2.9 In 2012-13, accounting alignment will be fully introduced across the public sector through the Government's Clear Line of Sight project, requiring spending plans, Parliamentary Estimates and expenditure outturns all to be reported in a consistent way. This will see the accounts of non-departmental public bodies and other central government bodies consolidated within the departmental Resource Account and Estimates.

2.10 These financial reporting innovations will improve the transparent reporting of public finances. But each places significant demands on government departments, local public bodies and their finance teams.

2.11 Substantial change to public audit will also result from the Government's decision to abolish the Audit Commission, with local authorities and others able to appoint their own auditors in future. Private sector audit firms, the National Audit Office and local public bodies will all be affected by these proposals still subject to Parliamentary approval.

An expert National Audit Office

2.12 Collectively, these policy, fiscal and audit changes have led departments and others to focus on core management and financial issues that underpin wider success in delivering complex and changing systems. Amid staffing reductions, managerial competence is at a premium, with a particular need for commercial skills to commission services and oversee contracts, and analytical and evaluation skills to determine whether local providers have delivered services for users. Public bodies will require thorough models of accountability, robust information systems that can allow for high-quality decision-making, an understanding of, and willingness to accept, controlled failure where necessary, and financial competence to implement structured programmes of cost reduction.

2.13 The National Audit Office has expertise in each of these areas. We draw on our extensive knowledge of the public sector to help government improve the way it manages its risks and its operations, as well as its information and its money; and to support Parliament as it holds government to account for delivering the best value for money for the taxpayer.

Part Three

Our impact

Summary

3.1 *Since 2009, we have implemented changes across our organisation to deliver the objectives set out in our strategy. These changes have helped us to improve our support to Parliament, to promote improvement, and to respond more effectively to the changing public sector environment. The results of these changes are now being seen in the quality and timeliness of our work and in our financial and wider impact.*

Developing our work

3.2 Accountability for public funds rests with Parliament. Our financial and value for money audit work helps Parliament to assess whether public money is used effectively. In the course of providing independent assurance on some 460 accounts and 60 major value-for-money studies each year, we highlight to Parliament important issues arising from our work that can help government to improve financial management and reporting.

3.3 The information that we provide enables Parliament and its Committee of Public Accounts to question departments as they design and implement projects. Over the last two years, we have developed additional ways of presenting our knowledge in order to respond to changing circumstances and to establish baselines against which departments can be held to account. In addition to our core value-for-money reports, we now provide Parliament with:

- **Landscape reviews**, which look across wide-ranging, complex or changing areas of government activity to build knowledge and expertise and to inform a Parliamentary and wider audience. Our landscape reviews have included reports on the health system and the government's Information and Communication Technology (ICT) capability.
- **Publications focused on government transformation.** The scale of the fiscal challenge has required departments to look beyond short-term savings and think more radically about how to cut costs over the longer term. We have developed a series of reports that highlight the key issues for departments to address when facing these challenges.

- **Work on accountability.** We have supported the work of the Committee of Public Accounts in exploring how accountability should operate as decisions about public services are increasingly devolved. We have also probed the issue in various value for money reports.
- **Financial Management reports.** A number of our reports have considered the financial maturity of departments, identifying key areas for improvement.

3.4 We have also developed more informal channels of influence, for example, by providing guidance to non-executive members of departmental boards, by supporting the chairs of departmental audit committees and by inviting finance directors to occasional events to discuss issues of relevance to their roles in government. In all this activity, we have endeavoured to use our knowledge and insight to provide departments with evidence and assistance in developing good governance arrangements, which are central to the achievement of value for money.

Our strategic themes

3.5 We have continued to focus on the three areas of weakness which, based on our assessment of departments in 2009, we concluded needed to be improved: financial management, cost-effectiveness and the use of information in government. Over the last two years, we have focused our work on promoting improvement in these areas, which remain central to the delivery of value for money across public services:

- **Good financial management and transparent financial reporting** are always crucial. Public bodies should have robust processes in place to manage their resources and risks effectively so that they achieve their goals and report spending comprehensibly to the public. In 2010-11, we assessed the progress that departments have made in developing their financial management. In the past year we have also worked with departments on how better risk management can help maintain high quality services in a time of cost reduction.
- Departments need **good quality management information to take decisions** in the design and delivery of services, as well as to track performance and control costs. In 2010-11, we assessed the standard of performance reporting to boards, and the quality and use of option appraisal in government. We validated the data systems underlying the input and impact indicators in departmental business plans, and we published value-for-money studies on formula funding and on the implementation of the Government's transparency agenda.
- In order to achieve the spending reductions required, **the challenge of how to achieve more cost-effective delivery** will continue to be a major focus for departments. Our work with audited bodies in 2010-11 focused on helping them to improve the quality of their decision-making and to drive waste out of their delivery arrangements. We analysed how departments managed their processes and delivered their services in order to influence their approach to service improvement.

3.6 These strategic themes continue to be important to public bodies over the coming year and will therefore remain central to our work.

Our objectives

3.7 We have also made progress towards our corporate objectives.

Build a high-performing NAO

3.8 In 2010, we set out our intention to reduce our costs by 15 per cent in nominal terms in the three years to 2013-14. Like the bodies we audit, we have had to assess our business model and choose our priorities. We have reduced staff numbers, frozen pay, and cut outsourcing and consultancy. In the year to 31 March 2011, we reduced our headcount by 3.1 per cent. In 2010-11, we also reduced our corporate costs by 5 per cent.

3.9 While implementing these reforms, we have maintained our commitment to quality and have delivered our work faster and more efficiently.

3.10 Our financial audit work is carried out by fully qualified accountants or those training for their professional qualification. Our audit work is independently assured annually by the Audit Inspection Unit. Those we audit tell us that they value our professionalism and actively seek our advice on accounting and financial issues.²

3.11 Our value-for-money work is undertaken by teams with skills in accountancy and social science disciplines. We have developed our in-house analytical capacity over the past year and in 2012-13 will continue to improve the quality and range of analytical tools at our disposal.

Develop and apply our expert knowledge

3.12 The NAO has access to extensive experience, knowledge and skills in central government audit, value-for-money analysis, financial management, performance measurement, and the cost-effective delivery of public services. Our remit gives us access to information from all areas of government, providing us with a unique cross-government perspective, as well as in-depth knowledge of each department or body.

² Moderated feedback from NAO clients conducted independently by Grant Thornton, 2011.

3.13 The huge amount of knowledge at our disposal must be marshalled and deployed effectively if we are to make the greatest possible impact. Over the first two years of our strategy, we have strengthened our knowledge base in ICT and systems analysis, economic analysis, and other specialist areas. We have developed our internal systems, using online tools to make it easier to find and share knowledge. We have established senior 'client leads' to consolidate our knowledge about the bodies we audit and to provide a high quality service to each of them. We have formed teams to analyse cross-cutting government issues that impact on all the bodies we audit. As a result of this activity, our staff reported in 2011 that they now find it easier to access the knowledge they need.³

3.14 We have made progress in establishing a knowledge infrastructure. But we still have more to do to exploit our knowledge effectively and bring clear benefits to the organisations we audit. In 2012-13 we will concentrate on ensuring that each front-line team has the knowledge it needs, both about individual audited bodies and about the collective expertise of the NAO, so that they are able to provide departments and other bodies with support that they can acknowledge as exceptional.

Influence public services

3.15 We can only drive lasting improvements in public services if our knowledge and expertise influences those deciding and implementing government priorities.

3.16 In 2011, our annual independent survey of senior staff across the organisations we audit⁴ confirmed that departments report high confidence in the quality of our work and are increasingly likely to turn to us for advice. They were positive about our own value for money and reported that our more diverse range of products provided them with knowledge and insight in relation to areas where they are facing tough decisions.

3.17 Our own external auditors have confirmed the impact that our work achieves. For example, our work on tax credits administered by HMRC led to reductions in error and fraud amounting to £569 million in 2009-10. Our work has led to long-term improvements in the quality of service provided to the public: our reports on stroke care (published in 2005 and 2010) and dementia care (2007 and 2010) made a series of recommendations that contributed to the development of new quality standards published by the National Institute for Health and Clinical Excellence. In 2010, our work led to identifiable, audited savings for government totalling in excess of £1 billion.

³ Findings from the 2011 NAO staff survey.

⁴ Moderated feedback from NAO clients conducted independently by Grant Thornton, 2011.

3.18 We also provide support to influential Parliamentarians, and particularly the Committee of Public Accounts of the House of Commons, who have a vital role in scrutinising government decision-making, and in holding departments to account for their programmes of activity. We have a dedicated team to assist Parliament by providing daily support to the Committee of Public Accounts and bespoke help to other select committees in both Houses, including by producing annual guides to our work on each of the 17 most significant government departments.

3.19 In 2011, an independent survey reported that 80 per cent of MPs felt that the NAO acted impartially and independently compared to other organisations.⁵ MPs also reported that the quality of our products and services was above average and improving. But the survey also revealed that some MPs want us to improve our communication with them. In 2012-13, we will address this by taking opportunities to provide briefing to MPs and select committees where our expertise coincides with their own interests.

⁵ Ipsos MORI summer survey of MPs 2011. Comparator organisations are HM Treasury, Office for National Statistics and Audit Commission.

Part Four

Building capability

Summary

4.1 *Over the coming year, we will further develop our ability to support Parliament and government in responding to the changing public sector environment. We will continue to work with departments as they implement significant changes to financial audit arrangements. We will also ensure that our value-for-money work rigorously focuses on the key areas of challenge for the public sector. While we will reduce our own costs further, we will strengthen our capability in order to respond to the challenge of undertaking new local audit work and we will ensure that we maintain high standards of quality by continuing to invest in our people.*

Delivering a quality audit

4.2 We will remain effective in addressing audit challenges. Over the last year, the first phase of the Treasury's Clear Line of Sight project was implemented, involving the production and audit of 'Trust Statements' for the first time. These statements are used to account for the revenue collected by organisations on behalf of the Consolidated Fund. The preparation and audit of these statements not only involved recording such transactions for 2010-11 but the restatement of the 2009-10 accounts.

4.3 More substantial changes are under way, with consolidated resource accounts being produced for the first time. These accounts bring together the income, expenditure, assets and liabilities of arms'-length bodies with those of the main department and its executive agencies, aligning those accounts with the budgetary regime under which departments operate. This will require substantial effort from departments and auditors, with major technical, accounting, system and logistical challenges to overcome.

4.4 We are meeting accounting officers to ensure that they are fully aware of the demanding timetable ahead, and we continue to support HM Treasury as they finalise their Financial Reporting Manual and illustrative accounts for the 2011-12 year. The result will be clearer financial information for departmental audit committees, the Committee of Public Accounts and for members of the public, improving the visibility and accountability of expenditure.

4.5 The local public audit landscape has also changed in the last two years. In August 2010, the Government announced its intention to abolish the Audit Commission. A procurement process is under way to move the provision of local audit entirely to the private sector, with contracts to be awarded in 2012 for the 2012-13 audits. Over the coming year we intend to develop our capacity to take on the role, should we be asked to, of developing the Code of Audit Practice, which defines the scope, nature and extent of local audit work. During 2012-13, the Audit Commission will continue to provide assurance on local accountability and our work will complement theirs.

Identifying value for money

4.6 We will produce 62 major value-for-money reports in 2012-13. We have previously published 60 reports each year. The two additional reports will focus on issues relevant to local government and the services they provide. We will work with local government bodies in developing our programme to complement their own sector-led improvement work. Our reports will draw on our knowledge of a wide range of issues facing the public sector and will reach conclusions on programmes overseen by individual departments as well as on cross-government activity.

4.7 We will retain our focus on improving financial management, the use of information in government and the cost-effectiveness of services, and on achieving financial and social impact from our work. Our studies will also look at the impact of departments' programmes on service users.

4.8 In 2012-13, we will continue to report on financial management in individual government departments, and will examine the effectiveness of internal audit across government. We will carry out work to support improvements in the quality and timeliness of departments' financial reporting, particularly in light of the revised reporting requirements and shorter timetable that implementing Clear Line of Sight requires for departmental annual accounts.

4.9 In 2012-13, we will consider and report on the information needs of government as it seeks to enhance user choice and extend transparency. We will explore how information should be managed in more devolved local delivery systems with different accountability models. In addition, we will continue to review the quality of the data systems underpinning the indicators in departments' business plans and work with departments to determine how they assess their cost-effectiveness.

4.10 Financial and performance information about public services is becoming increasingly accessible, in part as a result of the Government's drive for greater transparency. It is important that data can be compared between different bodies so that those responsible for delivering services can use information about others' performance to increase their own efficiency and effectiveness. Over the coming year, we will continue to support greater data comparability, for instance, by promoting examples of good practice and by ensuring that the data we gather ourselves are made available to the public.

4.11 Over the last year, we developed our ability to work with public bodies on their ICT and systems capability. Our reports, including our recent assessment of the National Programme for IT, have helped to define the challenges faced by the Government ICT community. In 2012-13, we will consolidate the impact already achieved and ensure that more of our staff are able to provide guidance to public bodies facing these challenges.

4.12 In 2012-13, we will continue to examine how government manages its processes and supports departments in implementing improvements and achieving more cost-effective delivery. We will also determine the extent to which departments learn from past experience when assessing whether new proposals can be delivered effectively and efficiently.

Responding to new challenges

4.13 We will ensure that our work in 2012-13 focuses on the key areas of challenge for the public sector.

4.14 The impact of the economic downturn, and the need for fiscal restraint, continue to shape all financial decisions made by the bodies we audit. Departments need to manage the risks involved in those decisions. In 2012-13, we will continue to examine and report to Parliament on the actions planned, and taken by, public bodies to address these challenges and reduce their costs.

4.15 Our work will address the wider issue of cost-effectiveness and examine the maturity of departments' financial decision-making, so that we can assess whether government is delivering value for money in a period of fiscal constraint.

4.16 More broadly, we will examine the Government's actions to address the economic downturn. We have already published reports on the stewardship of the wholly-owned banks and, until the fiscal climate changes, we will continue to keep Parliament informed of the financial liabilities to which public finances remain exposed.

4.17 Our programme will include further work on the financial support provided to banks partly or wholly owned by the Government. The assets, liabilities and contingent exposure on the Government's balance sheet as a result of this ownership remain significant, and are impacting on public sector borrowing. We will examine the management of these arrangements until they unwind, analysing whether the maximum possible return to the taxpayer is achieved.

4.18 We will also consider wider governance questions. As new providers enter the public service market and more funding decisions are taken by local bodies, the accountability and governance framework of the public sector will become increasingly complex. We will carry out work to explore how departmental accountability statements are working in practice and whether they provide adequate assurance that public money is appropriately accounted for. As accountability arrangements continue to evolve, we will consider the intersection of local and national delivery and accountability through our value-for-money programme. Our examination of shared service arrangements, which forms an element of our financial controls work, will contribute to this assessment.

Preparing for local audit reform

4.19 Over the coming year, we will respond to the specific challenges raised by the reform of local audit. In March 2011, the Government published a consultation document with some details of the new regime, but final plans are yet to be published and are still subject to Parliamentary scrutiny.

4.20 We are taking steps to be ready for a future role in local audit. We are planning on the basis that we will be responsible for setting the Code of Audit Practice, as proposed by government. We are also planning to undertake some value-for-money studies on issues relevant to local public bodies. Those issues might include how local government is working with national government to deliver national policies, such as in housing, as well as cross-sector issues including the financial resilience of local authorities.

4.21 We have held preliminary meetings with local government stakeholders about the changes to local audit. Our proposed role has been welcomed, particularly if we focus on systemic issues where our knowledge and understanding of good practice can help others. We will continue to engage with local government representatives as we shape our response to government reform.

4.22 We are also considering how our new local audit responsibilities can benefit Parliament. We anticipate being able to take a more holistic approach to public expenditure and to provide Parliament with a wider overview both of central policy decisions and of local spending decisions.

Supporting Parliament and government

4.23 In 2012-13, we will provide the Committee of Public Accounts with 62 major reports on value for money and, in addition, occasional topical briefings and 'landscape' reviews on significant policy challenges facing government.

4.24 We will continue to develop the range of products we provide to Parliament. There are 19 parliamentary select committees in the House of Commons that address government departments' work, as do committees of the House of Lords. We will brief them on issues relevant to their areas of interest in order to maximise the potential utility of our knowledge and audit findings, and will provide them with an annual review of our work with each department.

4.25 The bodies we audit say that we are a trusted authority in our core areas of expertise, but they want us to be more proactive in providing advice in between formal audits.⁶ We will achieve this by using our 'client leads' to act as a single point of contact to ensure that each body has access to the knowledge and expertise of the whole of the NAO.

6 Moderated Feedback from NAO clients conducted independently by Grant Thornton, 2011.

4.26 Our findings and recommendations should bring real benefit to audited bodies and to Parliament in scrutinising government. We will communicate with all stakeholders in ways that they find convenient and productive. We will look to utilise our back catalogue of audit findings more effectively by identifying opportunities where previous work is of current relevance.

4.27 In addition, we will improve our digital communications, through our website and other digital media, so that MPs and their researchers, civil servants and other public sector workers, as well as members of the public, have much easier access to our knowledge and analysis. This will all be done as part of our commitment to the highest standards of transparency.

Working with local and international partners

4.28 Local public bodies will become more interested in our work as we begin to address more local issues in our value-for-money studies and if, as currently proposed, we take on a role in setting the Code of Audit Practice. We have already met many senior local government stakeholders and valued the opportunity to hear their views. We will continue to undertake this informal consultation to develop our understanding of the issues facing local public bodies and to build solid links with the wider set of stakeholders that we will have in future.

4.29 We will continue to work with the other audit agencies across the UK in order to share our knowledge and to ensure that there is consistency in our audit work. We already play an active role in sharing our knowledge with audit offices overseas, including by receiving overseas delegations seeking to develop their knowledge and approach. We also help to develop the financial skills and practices of parliamentary staff in a number of countries. We seek to learn from international best practice and will continue to play an active role in shaping the international approach to public audit, including through our role on the UN Panel of External Auditors until 2016.

Remaining efficient

4.30 We are on track to meet our target to reduce our costs by 15 per cent in nominal terms over three years. Last year, we estimated this to be the equivalent of a 21.7 per cent real terms reduction if inflation is taken into account. Our Estimate for 2011-12 remains in line with our cost reduction plans and is 7.3 per cent lower than our forecast as at October 2010.

4.31 In 2012-13, we will reduce our costs by a further 4.7 per cent by reviewing the way we deliver our services and recover costs, by driving further efficiencies in our value-for-money work, continuing to reduce our corporate services budgets, and sub-letting our London office space.

4.32 In addition, we will increase productivity and performance by improving the consistency and quality of our products, by allocating staff more efficiently to projects, and by giving our auditors the knowledge, skills and confidence to continue to provide excellent services to the bodies we audit and to Parliament. Underpinning this will be our ability to retain and develop high-quality professional staff.

4.33 In 2012-13, we will continue to ensure that our internal systems and processes support our front-line staff in delivering an excellent service to Parliament and government. This will involve:

- planning our financial audit work to ensure we deliver high standards and low cost to audited bodies and value for money to Parliament for the resources invested in us;
- focusing rigorously in our value-for-money work on our core priorities of financial management, informed government and cost-effective delivery;
- identifying and prioritising other work that responds to the emerging risks faced by the bodies we audit;
- standardising our methodologies across teams to help us to develop best practice and reduce costs; and
- applying our knowledge of best practice to ourselves, so that we practise what we preach.

Our governance

4.34 The Budget Responsibility and National Audit Act received Royal Assent in March 2011, and will come into force during the current financial year. The Act establishes the NAO as a corporate entity and formalises the current governance arrangements, including the establishment of the NAO Board, which have been operating in shadow form since 2009. With a majority of non-executive members, the role of the Board is to support and advise the Comptroller and Auditor General in the exercise of his functions, and to provide oversight of NAO's resource management.

4.35 The Board brings independent insight, supports discipline and rigour in decision-making and ensures robust governance of our operations as we respond to the challenges of the coming years.

Part Five

Resourcing

Summary

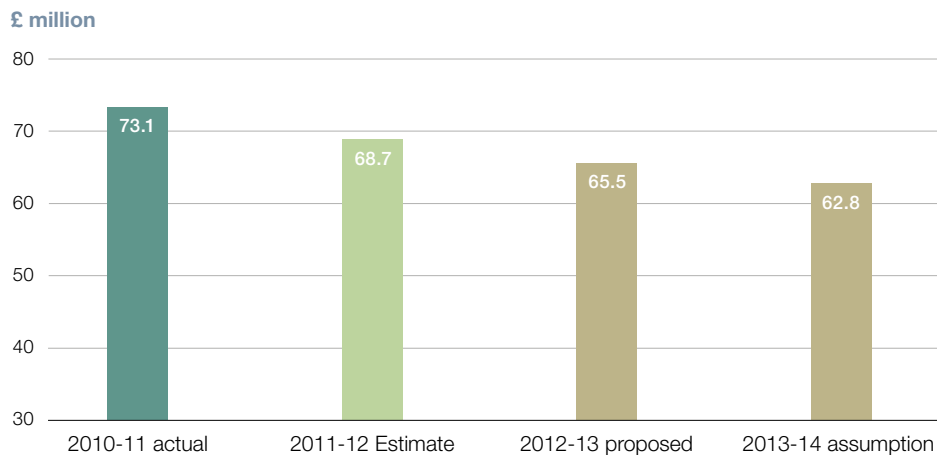
5.1 *We remain committed to reducing our costs by 15 per cent in the three years to 2013-14, but we are mindful of the external pressures on our costs. We will need to build our capacity to deliver the potential new responsibilities including those arising from the abolition of the Audit Commission, and we estimate that the net cost implications will be an additional £2.5 million in 2012-13. Our net resource requirement for 2012-13, excluding this new work, will however decline by 4.7 per cent from our 2011-12 Estimate to £65.5 million and we will continue to focus on maximising our own value for money.*

Working efficiently

5.2 We continually focus on reducing our costs and working more efficiently while maintaining quality, and we remain on track to achieve our target to reduce our costs by 15 per cent in cash terms in the three years to 2013-14 (see **Figure 2** overleaf) before taking account of new work. We proposed to the Public Accounts Commission last year that our net resource requirement should decline from £68.7 million in 2011-12 to £65.5 million in 2012-13. This is a reduction of 4.7 per cent, on top of the 7.3 per cent reduction in our Estimate for 2011-12.⁷ We remain committed to the resource requirements we set out last year.

⁷ See Note 1 overleaf.

Figure 2
Progress in reducing our costs



NOTE

1 Fifteen per cent reduction in our net resource requirement was based on our forecast as at October 2010, which was £74.1 million.

5.3 We plan to reduce our net resource requirement by 4.7 per cent in 2012-13 by driving further efficiencies in our value-for-money work and continuing to reduce our corporate costs budgets by 5 per cent. Further efficiencies in our financial audit work in 2012-13 will be counterbalanced by the increased demands of work on Clear Line of Sight. Our overall financial audit budget will therefore marginally increase.

5.4 We will achieve these further savings by:

- utilising staff more effectively while maintaining quality. We now have some 865 full-time equivalent staff, compared to 880 in 2010-11. Fewer than 17 per cent of our staff now work in back-office or support roles, with the majority working directly with the bodies we audit. We will reduce the number of full-time equivalent staff to 860 in 2012-13, excluding staff required to undertake new work, by completing planned reductions across our corporate services functions and by continuing to drive efficiencies in the delivery of our front-line work;
- reducing our outsourcing requirements. Having developed our in-house expertise in areas such as economic analysis, we will reduce our reliance on outsourcing to £13.2 million in 2012-13; and
- utilising office space better. By March 2012, we will double our annual rental income to £1.1 million as we sub-let another two floors of our London office space. We propose to sub-let further space by March 2013, producing a total annual income of £1.6 million and a total reduction in business rates of £0.4 million.

5.5 We remain committed to spending no less than 80 per cent of our resources on the delivery of our front-line services. We are on track to meet this target through:

- a three-year programme to review all corporate overhead costs and to maintain corporate service staffing levels at 16-17 per cent of total staff numbers;
- more integrated working across corporate service teams, making use of corporate service specialists to assist front-line work whenever possible; and
- annual reviews of all existing corporate contracts to rationalise services provided and renegotiate costs.

5.6 We are on track to achieve our cost reduction target and remain committed to doing so. But, in preparing our resource proposals for 2013-14, we are also conscious of the external factors beyond our control. Inflation, for example, currently stands at 5.2 per cent, which is double the rate when we set our initial budget and cost reduction proposals. In addition, the employment market for auditors is highly competitive, with salaries in financial services up 6.2 per cent this year. We wish to remain competitive in order to attract and retain high quality staff. We will monitor developments over the coming year and inform the Public Accounts Commission in autumn 2012 if we believe that our current resource proposals for 2013-14 should be amended.

Funding new work

5.7 In August 2010, the Government announced its intention to abolish the Audit Commission. The Government has since proposed that we take on from the Commission the role of setting the framework of auditing standards in the Code of Audit Practice. The Government also proposes that we assume responsibility for the audit of the 34 Probation Trusts across England. Probation services are funded directly by central government, so this change will allow these audits to align with our existing approach to central government finances. We anticipate that this change will take effect for the audit of probation trusts' 2012-13 accounts. We may also have a role in the audit arrangements for NHS Foundation Trusts.

5.8 With the winding-down of the Audit Commission's own value-for-money work, we propose to develop value-for-money studies that more explicitly address issues of relevance to local public bodies, particularly in local government. We intend to produce two studies of this type in 2012-13, increasing to four in 2013-14 and six in 2014-15, in addition to our existing programme of 60 major reports each year.

5.9 We are building our capacity to take on this work and we have recently appointed an Assistant Auditor General with extensive experience of financial management in local government.

5.10 This new work will generate additional costs. We remain committed to our existing cost reduction programme, so we have set out our resource requirements for this new work separately to ensure transparency and clarity between existing cost reductions and the additional costs associated with our new responsibilities. We will separately account for these additional funds and will return all unspent resources to Parliament if our costs are lower than currently envisaged.

5.11 We are working with the Government and the Audit Commission on our potential role in local audit, and we are informed by them on the potential costs of taking on the Code of Audit Practice and other responsibilities. As a consequence, we propose that the Public Accounts Commission should approve £2.3 million in 2012-13 to cover the cost of developing our approach to the Code of Audit Practice and the production of two additional value-for-money studies, as well as £100,000 set-up costs for our audit of Probation Trusts and any required work in Foundation Trusts. The cost of the actual audit of Probation Trusts will be covered by audit fee income.

5.12 We expect costs to rise over subsequent years as we move from developing to delivering the Code and to producing four then six value-for-money reports each year. The total additional resource requirements we anticipate in relation to work stemming from the abolition of the Audit Commission are set out in **Figure 3**.

Figure 3
Additional resource requirements for new responsibilities following the abolition of the Audit Commission

	2012-13 (£m)	2013-14 (£m)	2014-15 (£m)
Gross resource requirement	2.8	3.8	4.4
Income	(0.5)	(1.0)	(1.0)
Net resource requirements	2.3	2.8	3.4

5.13 In June 2011, the Treasury set out reforms to the financial regulatory system in its white paper, *A new approach to financial regulation: a blueprint for reform*. This included transferring responsibility for financial stability to two new Bank of England bodies, the Financial Policy Committee and the Prudential Regulation Authority, with responsibility for the conduct of business remaining with the new Financial Conduct Authority (FCA) as a successor to the Financial Services Authority (FSA). The proposed amendments also establish a statutory requirement for the NAO to audit the new FCA and its subsidiary bodies.

5.14 In preparation for these changes, which we anticipate will take effect for 2013-14 audits, we seek additional resources of £0.2 million in 2012-13 to plan for these new audit responsibilities and to enhance our financial services expertise. Our anticipated resource requirements for this new work over the next three years are shown in **Figure 4**.

Figure 4

Additional resource requirements for the audit of the Tripartite Financial Regulatory System

	2012-13 (£m)	2013-14 (£m)	2014-15 (£m)
Gross resource requirement	0.2	0.3	0.4
Income	–	(0.1)	(0.3)
Net resource requirements	0.2	0.2	0.1

Our use of resources excluding new work

5.15 In 2012-13, we will use 67 per cent of our resources to employ 860 staff, of whom more than 60 per cent are either trainee or qualified accountants. These figures exclude staff required to undertake new work.

5.16 In 2011, we recruited 80 trainees, comprising 70 graduates and 10 school leavers, and we will continue to invest in our professional training scheme over the coming year, seeking to recruit similar numbers in 2012. We will offer starting salaries for our trainees that are comparable with those of our key competitors. We cannot match accountancy firms in sponsoring high-potential undergraduates through university, but we will continue to promote the attraction of a career in public sector audit with the NAO.

5.17 We face increased pressure from financial and business sectors to retain the high quality staff we need, and we therefore plan to award modest increases in base pay for staff in 2012-13. The level of these awards will balance the need to remain competitive with the private sector with the pay restraint experienced by the bodies we audit. Given the reductions in our full-time equivalent staff, this pay increase can be managed within an overall reduction in our pay bill of £1 million in 2012-13.

5.18 We will continue to invest in developing skills to ensure that our staff have access to quality learning and development opportunities and remain at the forefront of their field in terms of professional standards. In addition, we have broadened our internal expertise by investing in our economic analysis function and our knowledge of large-scale government ICT. This has allowed us to drive our costs down by minimising our reliance on external contractors.

5.19 We receive support from a limited number of external partners to help us deliver our work. For example, we work with the private and academic sectors to gain assurance for our work. We will continue to ensure that optimum value is achieved from these arrangements by managing the support we receive from other organisations under strict contracts in order to ensure transparency and value for money at all times. Our outsourcing requirements will reduce by a further £2.5 million over the next three years.

5.20 **Figure 5** sets out how we propose to use our resources by type of expenditure. **Figure 6** shows our proposed use of resources by the type of work we undertake.

Figure 5

Analysis of resource requirements by type of expenditure

	2011-12 Estimate (£m)	2012-13 proposed (£m)	2013-14 assumption (£m)	2014-15 assumption (£m)
Staff	58.2	57.2	56.9	59.1
Outsourcing	15.0	13.2	12.0	12.5
Travel	3.3	3.1	3.1	3.2
Other cash costs	9.6	9.4	8.8	9.2
Non-cash costs	3.0	3.0	3.0	3.1
Gross resource requirement	89.1	85.9	83.8	87.1
Income	(20.4)	(20.4)	(21.0)	(21.0)
Net resource requirement	68.7	65.5	62.8	66.1

Figure 6

Analysis of resource requirements by type of work

	2011-12 Estimate (£m)	2012-13 proposed (£m)	2013-14 assumption (£m)	2014-15 assumption (£m)
Financial audit	47.6	48.0	46.9	48.7
Value for money	21.1	20.0	19.0	19.8
Performance improvement	10.2	8.1	8.1	8.4
Support for Parliament etc	9.9	9.5	9.5	9.9
Comptroller function	0.3	0.3	0.3	0.3
Gross resource requirement	89.1	85.9	83.8	87.1
Income	(20.4)	(20.4)	(21.0)	(21.0)
Net resource requirement	68.7	65.5	62.8	66.1

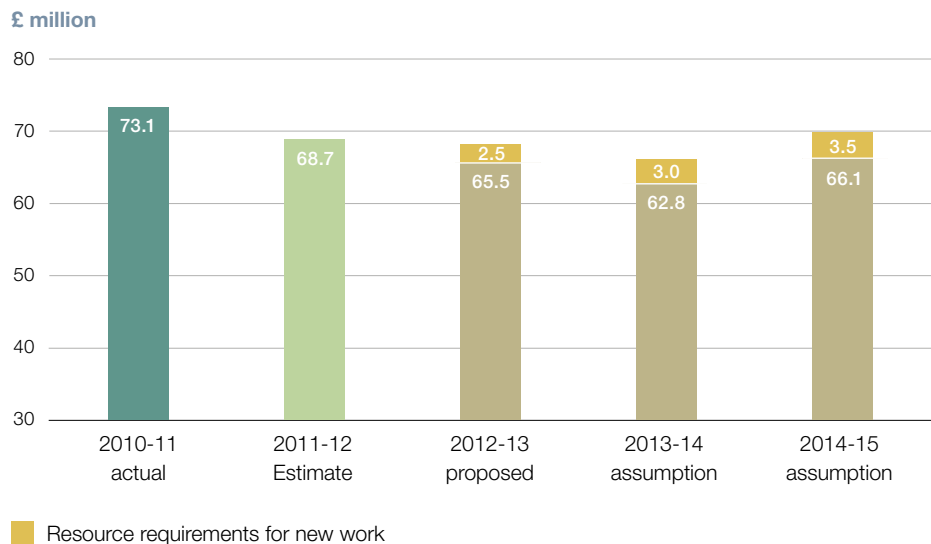
5.21 While we are on course to reduce our costs by 15 per cent by 2013-14, we now need to make planning assumptions for 2014-15. We expect the pressure on public finances to remain intense but we also need to continue to invest in the recruitment and retention of high quality staff following a period of pay restraint so that we remain an attractive career option for qualified accountants and other professional staff, particularly with inflation currently at 5.2 per cent. We have, therefore, planned for an increase of 4 per cent in gross budget terms in 2014-15. This will represent the first increase in the NAO's budget in four years.

Resource requirements including new work

5.22 The overall net resource requirement to fund our activities in 2012-13, including provision for new work, is £68.0 million. Our assumptions of resources required for 2013-14 and 2014-15 are shown in **Figure 7** and **Figure 8** overleaf.

Figure 7

Net resource requirements, 2010-11 to 2014-15

**Figure 8**

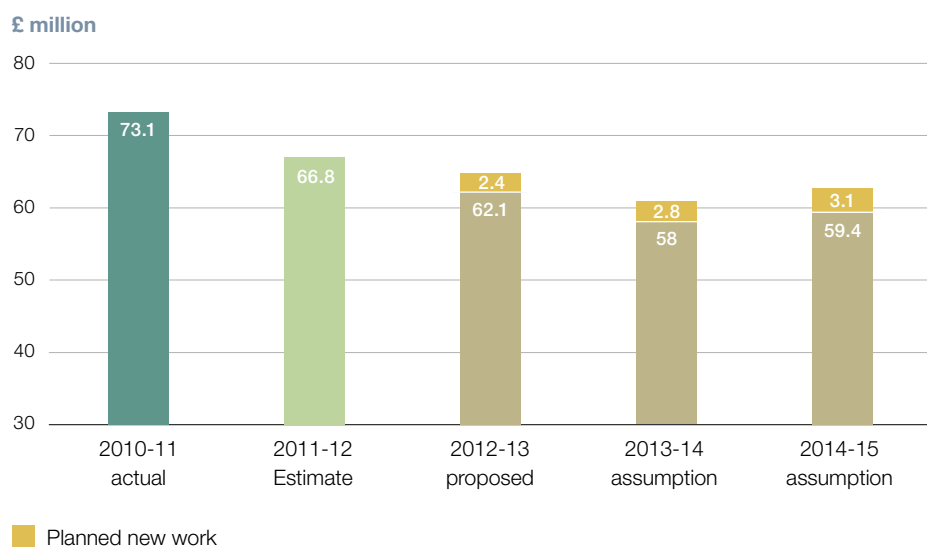
Net resource requirements including new work

	2011-12 Estimate (£m)	2012-13 proposed (£m)	2013-14 assumption (£m)	2014-15 assumption (£m)
Existing Work	68.7	65.5	62.8	66.1
New Work	–	2.5	3.0	3.5
Net Resource Requirement	68.7	68.0	65.8	69.6

5.23 Figure 9 shows that the real decrease in our core budget since 2010-11 equates to a 19.8 per cent reduction in real terms to the year 2014-15. While the impact of taking on proposed new work and the consequent additional resource requirements will have an impact on the scale of our real term reduction in costs, we still expect to make a real term reduction since 2010-11 of 15.6 per cent.

Figure 9

Net resource requirements: Budget movement in real terms, using GDP deflator

**NOTE**

1 GDP deflator applied from October 2010. 19.8 per cent reduction based on forecast as at October 2010, which was £74.1 million.

Capital expenditure

5.24 We propose to reduce our capital investment over the coming year by £0.1 million to £1.1 million (see **Figure 10**). This reflects lower capital needs to support our refurbished building, balanced against an increased use of IT to support flexible and remote working in the delivery of efficient audit and assurance services. We believe this level of investment is necessary to enable us to continue to provide modern and reliable equipment and audit tools in support of our work.

Figure 10

Capital provision 2011-12 to 2014-15

	2011-12 Estimate (£m)	2012-13 proposed (£m)	2013-14 assumption (£m)	2014-15 assumption (£m)
Capital provision	1.2	1.1	1.1	1.1

Part Six

Our performance

Summary

6.1 *Our work emphasises the need for our clients to use high-quality management information to inform effective decision-making. We apply the same requirements to ourselves. We have a range of measures in place to monitor our progress against our performance targets.*

Measuring our performance and impact

6.2 Last year we set out our proposals to update our public performance reporting framework in order to increase its alignment with our strategic objectives and to help Parliament and our other stakeholders to understand our work and how we are performing. We are now implementing this performance management framework. The measures we monitor are:

- **Our work saves public money.** We assess our financial impact,⁸ identifying savings across government achieved as a direct result of our work. In 2010, our work led to externally-audited savings to government of more than £1 billion.
- **Our work leads to positive change.** We look at the wider impact of our work and the work of the Committee of Public Accounts, including how we have influenced the way decisions are made to improve services. In 2010, we helped improve the management of asylum applications, influenced the way that government manages major projects, and contributed to quality standards for stroke and dementia care.
- **Parliament has confidence in the independent assurance and quality of work from the NAO.** We carry out an independent survey of MPs to understand the value of our work to Parliamentarians. In 2011, 71 per cent of MPs thought that the NAO brings about beneficial change, higher than for comparable organisations.⁹

⁸ Financial impacts arise where there is a direct link between our work and a beneficial change in an audited body. Full details of how our financial impacts are audited can be found in our 2011 Annual Report.

⁹ Findings taken from the 2011 Ipsos MORI summer survey of MPs. Comparator organisations are HM Treasury, Office for National Statistics and Audit Commission.

- **Clients acknowledge the value of our work.** A series of independent interviews are carried out each year with senior civil servants and chairs of audit committees to ascertain their views of our work. In 2011, 91 per cent of senior figures in government departments considered that our knowledge of central government finance is unrivalled, and reported that they would look to us to advise them on related issues.¹⁰
- **The NAO is a recognised authority in its core areas of expertise.** We undertake qualitative assessments of this measure, building on the stakeholder feedback we receive. Our most recent survey of MPs highlighted that 80 per cent of members view the NAO as impartial and independent.
- **We use funds cost-effectively.** We are on track to spend over 80 per cent of our resource on front-line rather than back-office activity, up from 76 per cent in 2010-11. We are also on course to reduce our overall costs by 15 per cent over the three years to 2013-14.

6.3 We expect to see high standards of transparency in financial and management reporting in the bodies we audit. We apply those high standards to ourselves. In the last year we have published information on all transactions over £500, as well as salaries and expenses of all senior staff. This information is available on our website.

6.4 Our progress towards achieving our strategy is set out each year in an annual report which also includes details of the impacts that we have achieved. Annual reports are available on our website and the next report, detailing our work over 2011-12, will be published in May 2012.

¹⁰ Findings based on analysis of data collated through the NAO moderated feedback programme which seeks the views of senior stakeholders from some 60 Government Departments and Agencies. Ninety-three per cent of Finance Directors interviewed strongly agreed or tended to agree that they would actively seek NAO advice on accounting and financial control issues.

