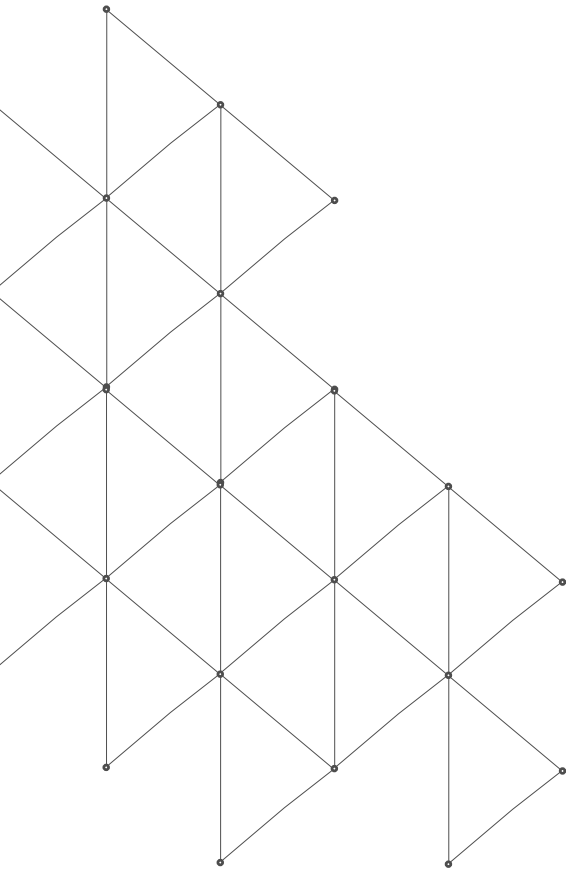




National Audit Office



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# Transparency Report

# **2017-18**

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JUNE 2018

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Our vision is to help the nation spend wisely.

Our public audit perspective helps Parliament hold government to account and improve public services.

The National Audit Office scrutinises public spending for Parliament and is independent of government. The Comptroller and Auditor General (C&AG), Sir Amyas Morse KCB, is an Officer of the House of Commons and leads the NAO. The C&AG certifies the accounts of all government departments and many other public sector bodies. He has statutory authority to examine and report to Parliament on whether departments and the bodies they fund, nationally and locally, have used their resources efficiently, effectively, and with economy. The C&AG does this through a range of outputs including value-for-money reports on matters of public interest; investigations to establish the underlying facts in circumstances where concerns have been raised by others or observed through our wider work; landscape reviews to aid transparency; and good-practice guides. Our work ensures that those responsible for the use of public money are held to account and helps government to improve public services, leading to audited savings of £741 million in 2017.

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National Audit Office

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# TRANSPARENCY REPORT 2017-18

This Transparency Report has been prepared to meet the provisions in the Statutory Auditors (Transparency) Instrument 2008 (the Instrument).

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This report can be found on the  
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# 2017-18: Our year in highlights

## **Our work informs debate**

We certified the accounts of all government departments, including big commercial entities such as the BBC, Network Rail and financial service companies, and many other public-sector bodies.

370 accounts certified covering more than £1.6 trillion of public income and expenditure.

65 major outputs published (value-for-money reports and investigations), including nine outputs on the government's preparedness for exiting the European Union.

The Committee of Public Accounts held 51 evidence sessions to tackle issues affecting the delivery of public services to the taxpayer.

We have begun planning for the work we will do in 2018 and 2019 to develop and consult on a new Code of Audit Practice due in 2020. The Code sets audit standards for some 950 local authorities and local NHS bodies and 10,000 smaller bodies such as town and parish councils. In addition we have published 13 outputs that included aspects of local services.

## **Our work affects people's lives**

Our major reports consider the user experience and make a real difference to people's lives. For example, our December 2017 study on the higher education market found that this market has yet to prove effective in driving improvements on price or quality. Our work directly influenced the development of the new regulatory regime, as well as contributing to the wider debate, with the Government launching a review of post-18 education funding in response. Our report also had influence in Parliament: it informed the Education Select Committee's inquiry into value for money in higher education, and the Treasury Select Committee drew directly on our study findings in its report on student loans, concluding that market mechanisms alone are not sufficient to drive improvements in quality.

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## **We deliver significant impact**

94% of recommendations in our reports discussed with departments, since April 2014, have been accepted.

Our briefing on Air Quality enabled an unprecedented four-way joint Parliamentary inquiry. It provided the committees with an understanding of why air quality matters and enabled MPs to question witnesses effectively and scrutinise the different policy options available.

Our work led to audited savings of £741 million in 2017. That's a saving of around £11 for every pound spent on running the NAO.

## **Our people are our greatest asset**

We care about what our people think and typically get excellent response rates to our People Survey (78% in 2017). This reflects how engaged our people are in wanting to improve the way we work as an office. The Board and Leadership Team take the survey very seriously and respond to any concerns raised, as well as building on successes.

We are a recognised provider for the ACA professional training scheme and our trainees achieved a 94% pass rate for the Professional Stage of the exams, beating the national average.

We are refreshing our Diversity and Inclusion strategy to make it more focused on achieving a diverse talent pipeline and creating an inclusive work environment.

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# Foreword from the Comptroller and Auditor General



We publish this Transparency Report at the height of our audit peak: some 300 accounts are being certified so they can be laid in Parliament ahead of Parliament's summer recess. Our portfolio of work means we audit £1.6 trillion of public income and expenditure. And in recent years, our core audit work has expanded to include big commercial entities such as the BBC, Network Rail and financial service companies.

Our work is driven by our obligation to provide independent, statutory audits on behalf of Parliament and our aim of driving public sector improvement.

We are in a unique position to comment on the effectiveness of accountability arrangements to Parliament, seeing the system from inside, while ensuring independence from those we audit. To continue to deliver high quality system-wide, integrated, independent public audit, which Parliament expects from us, we have been adapting to developments in the audit environment in line with the best of the audit profession. This has meant continuing to invest in our in-house IT audit capability, increasing our expertise in identifying and testing automated controls and developing our people's skills through training.

For our non-financial audit work to address the issues that matter most to government and Parliament, this has meant working with increasing agility. We have published 65 major outputs, including evidence based analysis of the government's preparedness for exiting the European Union. The oversight which NAO's work provides has never been more important and sometimes involves the NAO highlighting to Parliament that resources are inadequate for the task.

We also focused our efforts on responding to feedback from public bodies for further cross-government best practice and deepening the way we engage with those we audit. This deeper engagement has started to be reflected in the way accounting officers talk about our work including in areas where they may not have appreciated the value before.

Looking ahead, our work will continue to change as the regulatory environment changes following the UK's departure from the European Union. This will occur in an audit environment that is also changing. The introduction of new financial reporting standards will have a major effect on accounts, and we are talking with those we audit to ensure they are fully aware of the implications.

Our Annual Report and Accounts for 2017-18 sets out our performance during the year. This Transparency Report complements our Annual Report and Accounts by showing how our audit work has met the highest professional standards expected of us and made a significant impact during the year, both in terms of public sector improvement and transparency in the way public funds are spent, on behalf of taxpayers.

**Sir Amyas C E Morse KCB**  
Comptroller and Auditor General



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# Part One

## OVERVIEW

**1.1** This section provides an overview of the National Audit Office (NAO). It sets out our purpose, our work and the impact of our work.

### About us

**1.2** The NAO is the statutory auditor of government departments and a range of public bodies. We report to, and are funded by, Parliament.

**1.3** We audit the financial statements of all central government departments, agencies and other public bodies. Our value-for-money studies evaluate the economy, efficiency and effectiveness of government spending.

**1.4** The head of the NAO is the Comptroller and Auditor General (C&AG), who is an officer of the House of Commons and a Crown appointee. Both the C&AG and his staff are independent from government. We report objectively and independently on what the government does and we do not advise on policy objectives.

**1.5** We are a body corporate established under the Budget Responsibility and National Audit Act 2011.

### Comptroller and Auditor General

**1.6** The C&AG is appointed by Her Majesty the Queen as an Officer of the House of Commons. He is appointed for a single non-renewable term of 10 years and can only be removed from office by the Queen on an address by both Houses of Parliament. The C&AG has extensive statutory rights of access to information held by a wide range of public sector organisations. The C&AG's inspection rights extend to the records of many contractors to central government and those who receive public money from entities he audits.

**1.7** To preserve his independence from government, the C&AG has complete discretion in carrying out his functions. Responsibility for all audit opinions and judgements rests with the C&AG alone. The C&AG is also the chief executive officer and Accounting Officer of the NAO and is accountable to Parliament for operating the NAO and how we use public money. In carrying out the statutory duties of the post, the C&AG is supported by an executive Leadership Team and statutory Board, which set our strategic direction. A parliamentary committee, the Public Accounts Commission, oversees our work, appoints our external auditors, and scrutinises our performance. There is further information on our governance and structure in Appendix One: Governance and accountability.

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## Our work

**1.8** Our work is driven by our broad obligations to provide independent, statutory audits on behalf of Parliament and our aim of driving public sector improvement. Our work is always based on evidence, enabling us to form an opinion whether the financial statements of a public body present a true and fair view of the financial position and performance of the body in accordance with the statute, charter or other regulatory framework which underpins it.

**1.9** A focus on the evidence also allows us to get to the heart of why a programme or project underperformed or what made it successful. By comparing performance and insights between organisations and sectors, we detect systemic issues of wider importance, and identify good practice and lessons to be learnt.

**1.10** What sets us apart from private sector audit firms is that we can strive to provide system-wide, integrated and independent public audit.

- 'System-wide' because the breadth of our remit gives us an opportunity to look across the public sector and beyond organisational boundaries.
- 'Integrated' because financial audit and value-for-money audit work can together provide Parliament with a fuller, broader and deeper understanding of the challenges facing the public sector.
- 'Public audit' because the NAO and the C&AG are statutorily independent, and this ensures our work provides an independent voice for the public interest represented by Parliament.

**1.11** System-wide, integrated public audit can help to drive better public services for all. By looking across the public sector, one audit judgement building upon another with a clear view of the public interest, our role can be, and indeed should be, more than just driving accountability. It has the power to help public servants identify good practice, to help Parliament to understand better the practical effects of policy and to help government draw better connections between its decisions.

## Financial audit

**1.12** The C&AG, with the support of the NAO staff, provides an independent audit opinion on some 370 individual accounts across the public sector, including the major government departments. The scope and nature of our audit work is defined by international standards in auditing. In the course of our audit we can also identify areas where management may improve their controls or processes.

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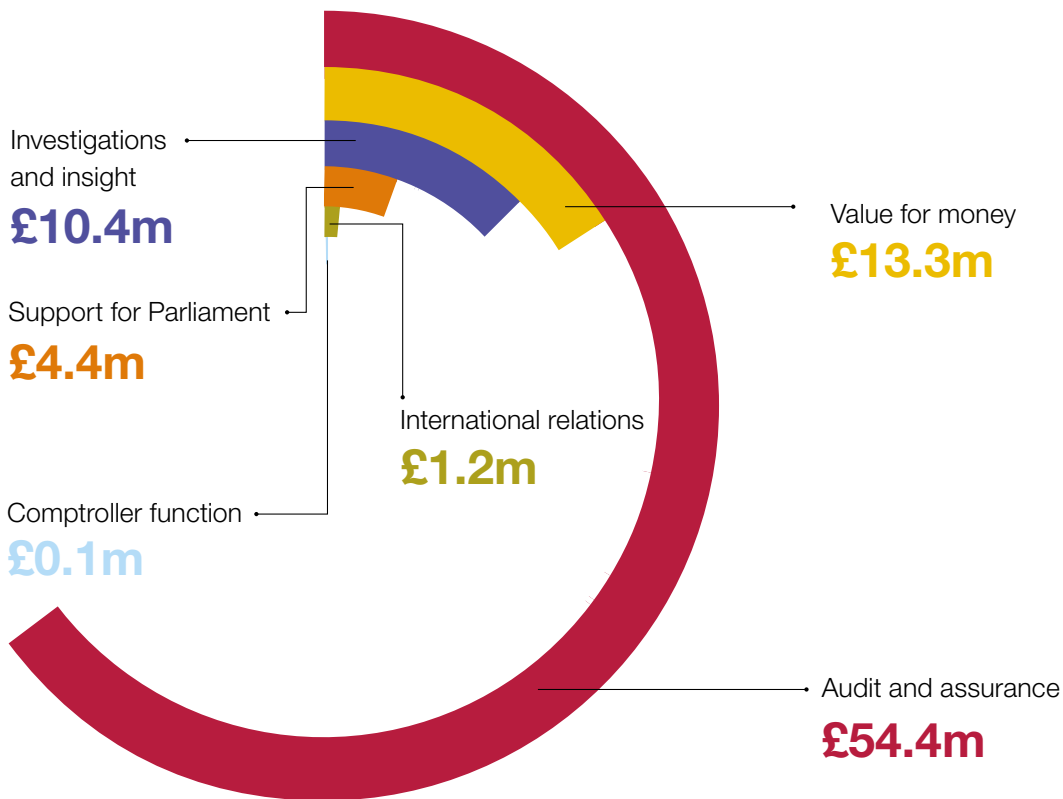
## Wider assurance work

**1.13** In addition to our financial audit work, the NAO carries out a wide range of other work to support Parliament in holding government to account. This includes:

- **Value-for-money work:** We examine the value for money – efficiency, effectiveness and economy – with which public bodies use their resources. Typically this focuses on a specific area of government expenditure and seeks to reach a judgement on whether value for money has been achieved. We also make recommendations on where improvements to public services can be made.
- **Investigations:** We conduct investigations to establish the facts when people or our work identify concerns about the use of public funds. Our investigations give a rapid and timely account of a situation or issue. To enable us to make this evidence available quickly, investigations do not seek to conclude on value for money.
- **Support for Parliament:** We support Parliament to hold government to account, supporting, in particular, the Committee of Public Accounts, other select committees and individual MPs in their scrutiny of public spending and delivery. The Committee of Public Accounts considers most of our value-for-money reports, and some of our investigations and financial audit work, in evidence sessions at which committee members take evidence from the senior officials of the organisations under scrutiny. The Committee of Public Accounts then typically publishes reports, including recommendations, the implementation of which is monitored and reported.
- **Local public services:** We report on the value for money of public spending locally, under the Local Audit and Accountability Act 2014. We are also responsible for the Code of Audit Practice, which sets out what local auditors need to do to meet their statutory responsibilities.<sup>1</sup>
- **Correspondence:** We deal with a high volume of correspondence from members of the public and MPs, representing a key point of direct contact. Coupled with intelligence from our work, correspondence is useful for bringing issues to our attention. It can lead to investigations or value-for-money studies.
- **International work:** The C&AG is the appointed external auditor of a number of international bodies. In addition, as one of the world's leading public audit offices, we participate in a number of professional standard setting groups under the umbrella of the International Organisation of Supreme Audit Institutions (INTOSAI).

<sup>1</sup> National Audit Office, *Code of Audit Practice*, April 2015. Available at: [www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2015/03/Final-Code-of-Audit-Practice.pdf](http://www.nao.org.uk/code-audit-practice/wp-content/uploads/sites/29/2015/03/Final-Code-of-Audit-Practice.pdf)

## The range of our work 2017-18



### Snapshot of our work

1.14 During 2017-18 we have:

- delivered audit opinions on some 370 individual accounts across the public sector, including the major government departments;
- published 65 wider assurance outputs;
- supported 51 Committee of Public Accounts evidence sessions;
- responded to 877 items of correspondence from the public and provided 108 responses to correspondence from MPs; and
- secured the appointment as the external auditor of the World Intellectual Property Office and the Pan American Health Organization. In addition the C&AG was elected as chair of the United Nations Panel of External Auditors.

1.15 Detailed information on our performance is contained in our annual report and accounts, available at: [www.nao.org.uk/report/nao-annual-report-and-accounts-2017-18](http://www.nao.org.uk/report/nao-annual-report-and-accounts-2017-18).<sup>2</sup>

<sup>2</sup> National Audit Office, *Annual Report and Accounts 2017-18*, HC 1128, Session 2017–2019, 26 June 2018.

# OUR VALUES

Our values underpin everything we do. We are:

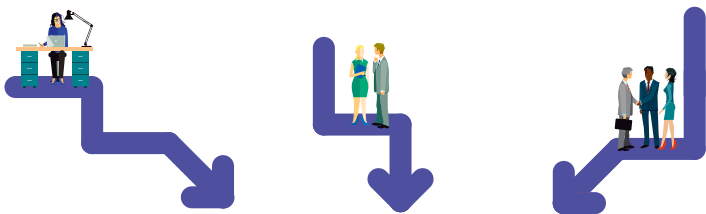
## INDEPENDENT

and objective, observing the highest professional and personal standards.



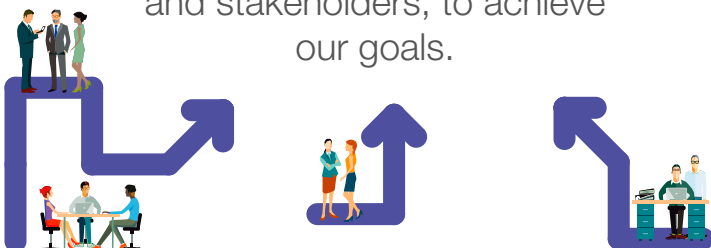
## AUTHORITATIVE

in delivering work of the highest quality, drawing comprehensively on robust evidence and practice.



## COLLABORATIVE

in our work with colleagues and stakeholders, to achieve our goals.



## FAIR

and just in our work and the way that we treat people.



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## Impact of our work

**1.16** Each year we identify cases where our work or influence has contributed to better public services, or a financially quantifiable net benefit to the taxpayer. We refer to this as our 'impact'. Our 2017-18 Annual Report and Accounts highlights 13 case studies illustrating the wider impact brought about through our work, for example improving patient access to general practice, local support for people with learning difficulties, and the working of the higher education market. These wider impact case studies have been approved by the bodies to which they relate.

**1.17** In addition, during calendar year 2017, the financially quantifiable impact of our work was £741 million which represents a saving of around £11 for every pound we spend. The audited bodies concerned also confirm these financial impacts and our external auditor gives assurance on them. A full list of our impact including our statement on financial impacts is available on our website: [www.nao.org.uk/report/nao-annual-report-and-accounts-2017-18](http://www.nao.org.uk/report/nao-annual-report-and-accounts-2017-18).

**1.18** We also monitor Treasury Minutes documenting the government's response to Committee of Public Accounts recommendations. We further monitor and discuss regularly with departments the implementation of our own recommendations across government as an additional measure of our impact. This helps to identify systemic issues and serves to further focus our work. The response rate to recommendations arising from our work is detailed in our annual report, available at: [www.nao.org.uk/report/nao-annual-report-and-accounts-2017-18](http://www.nao.org.uk/report/nao-annual-report-and-accounts-2017-18).

**1.19** An important quality measure for our work is how much it supports our objective to help Parliament hold government to account and improve public services. We commission independent qualitative interviews with senior civil servants and chairs of audit committees, and we use this feedback to undertake continuous improvement in our practice and our communications with departments.

**1.20** The bodies we audit remained satisfied with the NAO. Ninety-four per cent of survey respondents agreed that their relationship with us was good or very good. Respondents have a high regard for our financial audit work, with 88% agreeing it is of high quality and 88% saying that they would actively seek our feedback on accounting and financial control issues. This feedback is inline with that in 2016.

**1.21** Of those respondents directly involved in value-for-money studies (61 people), around seven in 10 rated the quality of their most recent value-for-money study as good or very good. Around 70% also agreed that their most recent study aligned with their organisations' strategic priorities and covered the right issues. A majority, 59%, said our value-for-money work overall brings valuable insights for their organisation, with 13% disagreeing. This feedback is also in line with that in 2016.

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**1.22** Overall, 55% of respondents said the NAO's recommendations led to improvements and 61% that during the NAO's work with them they had made changes prompted by the NAO's engagement.

**1.23** Since 2010, we have participated in the annual Ipsos MORI omnibus survey of MPs, to be sure that our work continues to meet their needs and to identify areas for improvement. The results of the 2017 survey show that our reputation among the MPs surveyed remains strong. The majority of MPs (nearly eight out of 10) across Parliament are familiar with us, or at least know a fair amount about us. This is well above average compared with the public and private organisations measured on the survey.

**1.24** In response to direct survey questions:

- 88% of MPs surveyed rated us as above average for being authoritative;
- 80% rated us as above average for being impartial and independent; and
- 77% rated us as above average for acting with honesty and integrity.

### **Adding value through our audit work**

**1.25** We are now developing a programme of more active engagement with those we audit to recognise and promote the insights from our work and to ensure we share our work with those who need it. As our audited bodies face new challenges, such as cyber security, or continue to address issues in financial reporting, our aim is to build a better understanding and engagement with them.

**1.26** We are starting to see this deeper engagement reflected in the way Accounting Officers talk about the work of the NAO, both in terms of our value-for-money work and our financial audit, including in areas where senior officials may not have appreciated the value before. For example, in October 2017 in giving evidence to the Committee of Public Accounts regarding the qualification of the HS2 Ltd financial statements, HS2 Ltd CEO, Mark Thurston told the Committee how he valued the work the NAO had done in identifying control weaknesses in the organisation. He said "we have accepted all the NAO's recommendations around our end-of-year accounts. We are putting most of those actions in place – many of them are already complete". He went on to say "we continue to meet the NAO every month, so they can see the measures we are taking to put corrective action in place to deal with some of our controls issues. We found the NAO Report really helpful".

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# Part Two

## AUDIT INDEPENDENCE AND QUALITY

**2.1** This section describes the importance of our independence, and our methods of training, quality assurance and quality monitoring.

### Independence

**2.2** For our work to have the impact and influence required, we must uphold high standards of ethics and probity, and work within a framework of values that preserve audit independence.

**2.3** We expect staff to adhere to the relevant internal and external quality standards for our work. For 2017-18, this includes:

- International Standards on Auditing (ISAs) (UK);
- our standards for value-for-money and non-financial audit work;
- the Financial Reporting Council's Revised Ethical Standard 2016 (the Ethical Standard), in so far as these can be applied to a statutory public sector audit body; and
- International Standard on Quality Control for audits (ISQC 1).

**2.4** The Directors of Financial Audit and value-for-money Practice and Quality are responsible for ensuring compliance with the relevant quality standards for their respective specialisms and for creating a culture of professionalism, rigour and openness to challenge.

**2.5** The Comptroller and Auditor General (C&AG) is the designated ethics partner (as defined by the Ethical Standard). His independence is enshrined in statute. We are alert to areas where the National Audit Office (NAO) or our engagement teams' independence and objectivity could be, or perceived to be, threatened. All staff must attend training to ensure that they understand the ethical and professional standards with which they must comply. An annual declaration is required by all staff to confirm that they are aware of their ethical and professional obligations.

**2.6** We set up strong safeguards against threats to our independence. We are appointed to most audits (including value-for-money audits) by statute. This means that the audited entity cannot replace us as auditor in response to negative audit opinions. Moreover, we do not seek to profit from providing non-audit services to clients. This removes threats to independence that could arise from an auditor seeking to protect non-audit income.



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**2.7** Where appropriate, we fully implement the Ethical Standard's safeguards. For example, to prevent over-familiarity of audit staff with the client, we regularly rotate senior staff on financial audit in line with the requirements of professional standards. Detailed procedures for identifying potential threats to independence and establishing appropriate safeguards are embedded into our audit methodology.

## **Our people**

**2.8** We deliver high-quality work because we invest in recruiting, developing and retaining the right calibre people. The vast majority of NAO staff working in financial audit are either Consultative Committee of Accountancy Bodies (CCAB) qualified or in training for a CCAB qualification. In addition, we use specialists to support audit teams, for example statisticians and IT specialists. Many staff engaged on value-for-money audit also trained with us as accountants. We also recruit analysts and senior analysts in many specialist analytical disciplines, including economics, statistics, social research and operational research.

**2.9** Our largest sources of talent are our graduate and school leaver programmes, with 62 people recruited to our graduate scheme and eight to our school leaver scheme in 2017. Ninety four per cent of our trainees passed the Professional Stage examinations for the Associate Chartered Accountant qualification at the first attempt (compared with 83% nationally) and 85% passed the Advanced Stage examinations at the first attempt (in line with the national average).

**2.10** The professional accountancy training for staff is supplemented by in-house training in both financial and value-for-money audits. All frontline staff working on audit must attend an annual assurance update and have further training on specific areas such as leading for audit quality.

**2.11** On average, staff undertook 6.4 days of structured training during 2017-18. This includes training in areas of specialist accounting and central government audit.

## **Financial audit**

**2.12** All financial audit staff have access to a wide range of financial audit training, in addition to an annual assurance update. In 2017-18 we enhanced the technical and professional training available, particularly introducing a programme on 'leading quality' for all directors, managers and audit leads. Other training can be selected based on the individual's role and prior experience. For example, targeted training was provided in the following areas:

- the auditing of accounting estimates;
- the auditing of pensions schemes;
- the auditing of charities;
- group audits; and
- new accounting standards IFRS 9 and IFRS15.

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**2.13** In response to feedback from trainees that commented on the shift from a three-year training programme to support them before they qualified to a post-qualification situation, we have introduced a two-year programme that is designed to support audit principals and senior analysts moving into a lead role on audit engagements. This programme consists of existing learning and development offerings and includes elements such as essential skills for new managers, workshops and opportunities to develop other, non-audit skills that will help colleagues get better at their job. The programme is also available to colleagues engaged in wider assurance work. This provides good opportunities for collaboration across the disciplines.

### **Value-for-money and investigations**

**2.14** Staff engaged in value-for-money and investigations are qualified accountants (or training in accountancy) or specialists qualified to Masters Level or equivalent in other disciplines such as economics, statistics, data science, social research and operational research. Over the past two years we have focused on strengthening our data analytical capabilities to enable us to strengthen the insights we can provide using data science. To maintain the technical competence of staff engaged in non-financial audit work, we give a full and varied training programme, ranging from introductory courses for trainees and new analysts to technical courses for experienced practitioners. We also expect our staff to provide peer-training and advice and support to the practice on the use of specialist skills and methodologies.

**2.15** Courses for trainees include among other topics:

- an introduction to assurance methods (incorporating both financial audit and value-for-money methodology);
- interview techniques; and
- statistics and research methods.

**2.16** Trainees also gain experience of value-for-money audit and investigations by working on these outputs alongside their financial audit training. We fund more complex technical courses run by external training providers and specialists where appropriate.

**2.17** We provide formal one-to-one coaching for people who wish to explore and address underperformance across any aspect of their work.

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## Office-wide skills strategy

**2.18** To ensure our people continue to be best placed to deliver high performance, we will be launching an ambitious new skills strategy later this year. The current strategy focuses on continuous professional and technical development. It emphasises the importance of learning new skills on the job to ensure we develop expertise to support the consideration of the strategic issues across the range of our audit bodies. We seek to disseminate this expertise across the NAO by promoting collaboration and knowledge sharing. We also support our people to acquire other relevant qualifications, such as those offered by the International Association for Contract and Commercial Management, the Diploma in Corporate Finance and the Institute of Leadership and Management coaching qualification.

**2.19** We have rolled out a training course to everyone in the office under the name 'The Way We Work'. The programme supports people in developing their personal, management and team-working skills.

## High-quality performance

**2.20** Financial audit conforms to International Standards on Auditing (UK). Our value-for-money assurance work is more varied, consistent with our VfM standards, while also being responsive to the needs of many audiences in government and Parliament. Our wider assurance work can range from traditional value-for-money reports evaluating major projects after the event, to early looks at major programmes, to landscape reviews of particular policy areas, and briefings on specific issues. It also includes our investigations to establish the facts when people or our work identify concerns about the use of public funds. Our investigations give a rapid and timely account of a situation or issue.

## Financial audit

**2.21** All our financial audit work complies with auditing standards. The C&AG must perform certain discretionary audits under the ISAs (UK), and he has chosen to adopt these standards for all financial audits. These standards include International Standards on Quality Control 1 (ISQC 1 (UK)). Meeting these standards means that our financial audit work also complies with the relevant International Standards for Supreme Audit Institutions (ISSAIs) established by the International Organisation for Supreme Audit Institutions (INTOSAI).

**2.22** We engage widely with the accountancy and auditing professions, through the professional institutes, with other UK and international public audit bodies and through our private sector framework partners. This helps us to share good practice and learn from other practitioners. We engage with the partnership firms to keep in touch with developments across the wider profession and to ensure our methodology remains in line with best practice.

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**2.23** In addition, the NAO and its staff are appointed to a wide range of professional bodies and committees including: the Financial Reporting Council's Audit Technical Advisory Group, the Council of the Institute of Chartered Accountants in England and Wales (ICAEW) and relevant ICAEW boards and groups, the Council of the Chartered Institute of Public Finance and Accountancy (CIPFA) and relevant CIPFA boards and groups, HM Treasury's independent Financial Reporting Advisory Board and INTOSAI. These appointments seek to ensure that the public sector perspective is properly reflected in developments within the accounting and auditing profession.

**2.24** Our audit methodology is outlined in our *Financial Audit Manual*, which is updated regularly. This complies with the requirements of the ISAs (UK) and provides guidance on interpreting and implementing those standards within the central government sector. Further details on our financial audit methodology and quality assurance processes are included in Appendix Two: Assurance and control.

**2.25** We build quality control into all stages of a financial audit to ensure that the work is of the highest technical quality. We extensively review our work and there are a number of specific review stages. All work undergoes a two-stage review by senior members of the engagement team. Some audits that include significant audit judgements undergo an engagement quality control review by an independent and experienced director. The allocation for this additional layer of review is dependent on the nature of the engagement, the identification of unusual circumstances or risks, the requirements of the laws and regulations and the size and complexity of the organisation. We place a premium on consultation-driven audit quality. Consultation meetings are held at the planning stage of our highest-risk audits and technical panels are convened to consider higher-profile qualifications, significant audit judgements and C&AG reports. These meetings and panels comprise our relevant executive leaders, our Director of Financial Audit Practice and Quality and senior engagement team members.

**2.26** In addition, we complete an annual quality assurance programme to make sure that we comply with the *Financial Audit Manual* and International Standards on Auditing (ISAs). Our Compliance and Quality Unit, which reports to the executive Leadership Team, coordinates a programme of hot and cold reviews that are completed before and after an account is certified respectively.

**2.27** The findings of these reviews show where audit quality has improved, as well as further areas to address. We communicate areas for improvement to all financial audit staff through regular bulletins, our mandatory annual technical update and, where appropriate, incorporate them into further guidance, training and embed them into our methodology.

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**2.28** We have also introduced root-cause analysis to understand more deeply any areas in our work where we have identified scope for improvement in order to identify how we can strengthen further our audit practice. This helps us to identify transferable learning for the wider audit practice, which we disseminate through training and support on thematic issues, including targeted training for those new to supervising or overseeing financial audits. Further details on the review and assurance processes and our actions to address areas for potential improvements to audit quality are set out in Appendix Two: Assurance and control.

**2.29** Audit quality forms a key part of our financial audit performance management framework. Failings and good practice in audit quality are reflected in the performance assessment of directors and their teams.

**2.30** In order to make sure we keep up with developments in financial audit, in 2017-18 we appointed a Director for Operations and Financial Audit Development. The role includes two key responsibilities with a focus on quality. Firstly, the director is responsible for making sure our audit teams have the resources they require to perform quality audits, and secondly the director is responsible for considering how we continue to develop financial audit so that our methodology stays fit for purpose into the future.

### Value-for-money and investigations

**2.31** We expect staff engaged in value-for-money studies and investigations to meet our standards for value-for-money and other non-financial audit work (VfM standards). These standards stipulate clear quality-review requirements and responsibilities within audit teams.

**2.32** Our standards set out the mandatory principles that all non-financial audit work must meet, together with the guidance on current approaches to implementing the standards. These standards are based on current best NAO practice and they are consistent with the Fundamental Auditing Principles of the International Standards of Supreme Audit Institutions (ISSAIs), tailored to meet the specific expectations and requirements of the UK public sector environment and Parliament. They are accompanied by a more detailed explanation of current approaches to implementing the standards. Further details on the standards are set out in Appendix Two: Assurance and control.

**2.33** Value-for-money studies and investigations are subject to a multi-stage quality assurance process involving a core of mandatory elements. We carry out an internal review of a sample of our audit outputs to check adherence to mandatory processes. We also subject a separate sample to external review (see Appendix Two: Assurance and control for further information). Our internal cold review process checks adherence with the VfM standards and identifies and disseminates lessons to improve our practice.

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## Quality control

### Leadership Team

**2.34** The C&AG is supported by an executive Leadership Team which meets weekly and provides executive management and governance to the operations and delivery of the NAO's objectives.

**2.35** The responsibility for the NAO's system of quality control ultimately rests with the C&AG. The financial audit executive leaders are the Leadership Team members responsible for financial audit quality, reporting to the C&AG, the wider leadership team and the Board as appropriate. The financial audit executive leaders lead the Financial Audit Directors' Group, which comprises all financial audit directors and which has an oversight role for the quality of financial audit. Financial audit executive leaders and the Financial Audit Directors' Group are supported in their responsibilities by the Director, Financial Audit Practice and Quality.

**2.36** The C&AG and the Leadership Team are also supported by the Compliance and Quality Unit (CQU) and by quality directors within each cluster. The CQU has the key objective of monitoring compliance with professional auditing standards and the NAO's financial audit policies and the *Financial Audit Manual*. It also drives improvements in quality through review of audit work against best practice.

**2.37** For value-for-money audit, the C&AG and the Leadership Team are supported and advised by the Director of VfM Practice and Quality. The VfM Quality Group, which comprises value-for-money executive leaders and quality lead directors, advises the wider Leadership Team and provides oversight over all aspects of quality relating to the NAO's value-for-money and investigations work.

**2.38** Appendix One: Governance and accountability and Appendix Two: Assurance and control explain how we are structured in more detail.

### External monitoring for high-quality audit

**2.39** The Practice and Quality Team and the CQU consider and report the results of the external monitoring to the C&AG and the financial audit practice leadership team. Key findings are shared with colleagues across the wider financial audit and value-for-money practices.

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## External monitoring – financial audit

**2.40** Each year, the Financial Reporting Council's Audit Quality Review Team (AQRT) inspects our work.

**2.41** The AQRT are required to inspect the work which we complete under the Companies Act and we voluntarily invite them to inspect the work which we complete under other statute. In 2017-18, the AQRT reviewed seven of our audits: four Companies Act audits and three public body audits. The AQRT also carried out a cyclical review of the NAO's processes, policies and procedures supporting audit quality and a follow-up review of prior year findings. The sample of seven audits reviewed is a small, non-statistical sample. Although the sample is not statistically representative, it supports an independent review of our audit work, which informs our understanding of areas where we can make ongoing improvements in the quality of our work.

**2.42** We value the insights that the AQRT findings give us and we have taken action to develop our organisation-wide support to quality and our audit approach where appropriate. Further details of these monitoring arrangements, their findings and our responses can be found in Appendix Two: Assurance and control.

## External monitoring – value-for-money studies and investigations

**2.43** Each year, external specialists review a sample of published value-for-money reports and investigations. In 2017-18 Oxford Business Schools, Risk Solutions and RAND Europe undertook this work and examined 12 reports. The reviews considered the scope of the study, qualitative analysis, structure and presentation, graphs and statistics, methods used, synthesis of conclusions, recommendations (where made), systemic issues and overall perception.

**2.44** Overall, all reports met or exceeded our expected standard. The reviewers assessed reports as well structured and well written, with high ratings for how the team set the scope, objectives and evaluative criteria, and brought analysis and conclusions together. Reviewers noted some cases where we could have provided more details about our methodology and dealt more fully with systemic issues raised by our reports. Further details of these monitoring arrangements can be found in Appendix Two: Assurance and control.

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# Appendix One

## GOVERNANCE AND ACCOUNTABILITY

**1** Effective governance is vital to an organisation's success. We work to practise what we preach by upholding high standards of governance in our operations and decision-making. The Board supports and advises the Comptroller and Auditor General (C&AG) in meeting his statutory responsibilities and oversees how we manage and use resources.

**2** Our governance arrangements have been developed and implemented in accordance with the requirements of the Budget Responsibility and National Audit Act 2011. The arrangements reflect our unique statutory position and Parliament's wish that our governance should independently control and oversee our operations, while preserving the C&AG's independence in giving audit judgements.

**3** The National Audit Office (NAO) is accountable to Parliament via the Public Accounts Commission. The Public Accounts Commission's role is defined by both the National Audit Act 1983 and the Budget Responsibility and National Audit Act 2011. The Public Accounts Commission's principal duties under these acts are to examine the NAO's annual budget and lay it before the House, to consider our strategy, to appoint our auditor and receive their reports, to appoint non-executive members of the Board, and to report from time to time.

**4** Our Board has nine members, with a majority of non-executive members including the Chair. It provides rigour and discipline in decision-making and brings insights from the wider experience of the non-executive members to inform the strategic thinking of the NAO. The Public Accounts Commission appoints the non-executive members, except for the Chair, who is appointed by the Queen under letters patent, upon the recommendation of both the Prime Minister and the Chair of the Committee of Public Accounts. This ensures that the non-executive members are independent of our management, and that the Chair has the confidence of both the government and the opposition in Parliament. The relationship between the Board and the C&AG is set out in more detail in our Code of Practice.

**5** The Budget Responsibility and National Audit Act also requires that the C&AG sits on the Board, with three other executive members, who are nominated by the C&AG and appointed for a fixed term by the non-executive members.

**6** The members of the Board and Leadership Team are set out on pages 25 to 31.



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## The NAO Board and Leadership Team



Michael Bichard worked at senior levels in local government and was Chief Executive at Brent Borough Council and Gloucestershire County Council. He then moved to central government working as Chief Executive of the Benefits Agency and then as Permanent Secretary at the Department for Education and Employment. Since his retirement from the civil service in 2001, he has held a variety of positions including Vice-Chancellor of the University of the Arts London, chair of the Legal Services Commission, founder Director of the Institute for Government, chair of Shakespeare's Globe Theatre, chair of the

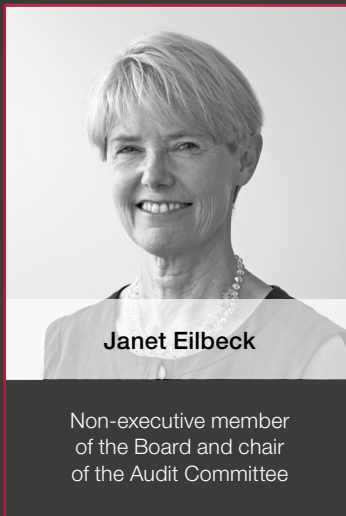
Design Council, and has recently retired as chair of the Social Care Institute for Excellence. He also chaired an enquiry into the Soham murders in 2004. Michael is currently chair of Bristol Business School Advisory Board, non-executive director at The Key (an education support company), and a Trustee of the River & Rowing Museum. He received a knighthood in 1999 and became a cross-bench member of the House of Lords in 2010. He was for five years Deputy Speaker of the House. Michael's first term of three years as Chair of the NAO ended on 9 January 2018. He has been re-appointed as Chair for a final three-year term of office.



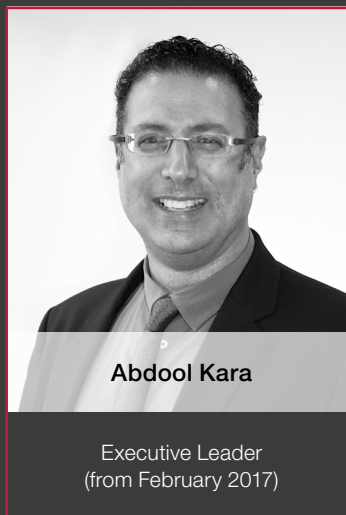
Sir Amyas Morse was appointed Comptroller and Auditor General on 1 June 2009, for a fixed non-renewable term of 10 years. Amyas is a member of the Institute of Chartered Accountants of Scotland. He was Global Managing Partner (Operations) at PricewaterhouseCoopers before he joined the Ministry of Defence in 2006 as Commercial Director. He has served as a member of the Major Projects Review Group and the Public Sector Board of the Chartered Institute of Purchasing and Supply, and on a National Health Service Project Board.

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## The NAO Board and Leadership Team



Janet Eilbeck is a Chartered Accountant with more than 30 years' experience. She was an assurance partner at PricewaterhouseCoopers until 2011, specialising in government and the broader public sector, including wide experience of internal audit. She was also chair of the Internal Audit Standards Advisory Board (IASAB), and the independent financial expert for the Department for Education and Employment. She has been a non-executive member of the Board and the chair of the NAO's Audit Committee since October 2016.



Abdool Kara was appointed to the Leadership Team as Executive Leader with strategic oversight of our work relating to local service delivery in February 2017.

Abdool brings a significant depth and breadth of experience from senior roles in local government and delivery of local services, as well as from his wider public sector accountability and inspection work. Before joining the NAO, he had been Chief Executive of Swale Borough Council since 2009.



Daniel Lambauer joined the NAO in 2009 as a performance measurement expert and helped establish our local government value-for-money team. Prior to his appointment to the Leadership Team in April 2017, he led the development of the NAO's value-for-money practice. Daniel is the Executive Leader with responsibility for the NAO's strategy and operations. Prior to joining the NAO, Daniel worked in a range of sectors, including academia, management consultancy and the civil service.

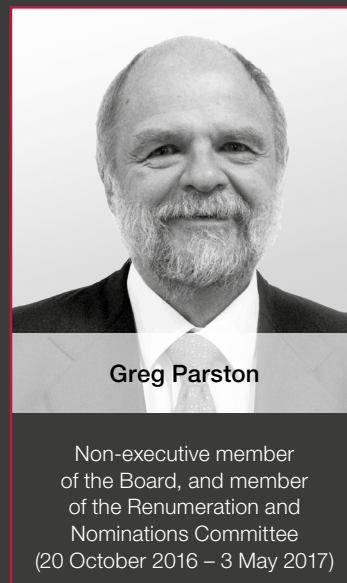
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## The NAO Board and Leadership Team



Kate Mathers joined the NAO in 2000 and joined the Leadership Team in April 2017 as Executive Leader with oversight of financial audit. Prior to her appointment to the Leadership Team, she led the development of the NAO's financial audit practice.

Kate is a Chartered Accountant with many years' experience auditing a wide range of public sector bodies. She held senior management positions in finance and operations while working on secondment at the Independent Parliamentary Standards Authority, and sits on the Institute of Chartered Accountants in England and Wales' (ICAEW's) Council.



Greg Parston was appointed to the NAO Board in October 2016 as a non-executive member. Greg is a senior manager and organisation consultant with strong skills in governance, strategy and change management. He has extensive experience in public service delivery and policy and has advised leaders in government, the civil service and charitable organisations around the world on how to improve social and economic outcomes.

Greg Parston is currently the senior adviser at the Institute of Global Health Innovation at Imperial College London and chair of Dartington Hall Trust. Greg resigned in May 2017 due to his increasing external and overseas commitments.

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## The NAO Board and Leadership Team



Rebecca Sheeran joined the NAO in 2004, and joined the Leadership Team in April 2017 as Executive Leader with oversight of value-for-money. She is a Chartered Accountant with many years' experience auditing a wide range of public sector bodies, covering both financial and value-for-money audit. Prior to taking up post on the Leadership Team Rebecca led the NAO's value-for-money audit of the Department for Transport and Network Rail, including work on modernising the Great Western Railway and progress with preparations for High Speed 2.



Ray Shostak CBE is an international adviser in education, government performance and public service reform. He has held a number of positions in local and central government, including head of the Prime Minister's Delivery Unit, and was a member of the Board of HM Treasury from 2007 to 2011. Ray is currently chair of Trustees of the Consortium of Voluntary Adoption Agencies, a Trustee of the Early Intervention Foundation and is an Honorary Norham Fellow at Oxford University. He has been a non-executive member of the Board and chair of the Remuneration and Nominations Committee since January 2015. Ray completed his first three-year term as non-executive member of the Board on 31 December 2017, and his appointment was renewed on 1 January 2018 for a final three-year term.

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## The NAO Board and Leadership Team



Stephen Smith joined the NAO in August 2015 as an Executive Leader. Before that, he had more than 20 years' experience as a partner with KPMG, where he led a number of initiatives for the firm, nationally and internationally. His experience ranges across a broad spectrum, including audit, mergers and acquisitions, and business advice, as well as a secondment to HM Treasury Accounting Group. Stephen is jointly responsible for leadership of the financial audit work-stream, a portfolio of public sector bodies and, more generally, the NAO's corporate finance-related work.



Robert Sykes OBE has significant experience of working in local government, and served as Chief Executive of Worcestershire County Council for 10 years. He has non-executive experience in the private and public sectors, most recently serving on the board of Core Assets and as non-executive member of the Board of the Crown Prosecution Service until 2012. In 2012, the Secretary of State for Communities and Local Government appointed him as lead commissioner at Doncaster Metropolitan Borough Council. He stepped down in the summer of 2014 when the intervention successfully ended. Robert is the NAO's Senior Independent Member. He completed his first three-year term as non-executive member of the Board on 31 December 2017, and his appointment was renewed on 1 January 2018 for a final three-year term.

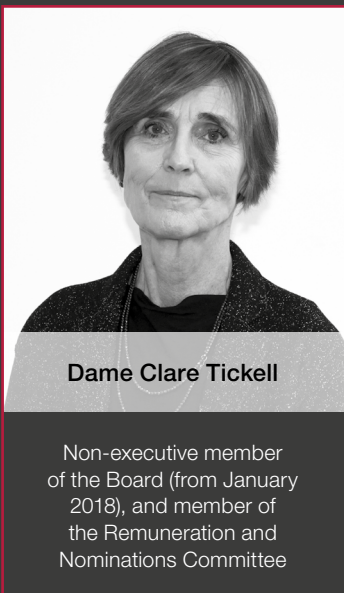


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## The NAO Board and Leadership Team



John Thorpe joined the Leadership Team in January 2014 and from April 2017 has been one of the Executive Leaders on the NAO Board. He has experience across a range of portfolios throughout his NAO career, including employment, agriculture, international and the NAO's technical team. As a director he was responsible for our financial audit of HM Treasury and HM Revenue & Customs. John currently shares the responsibility for the leadership of the financial audit work-stream and NAO's international work.



Dame Clare Tickell has extensive experience at board level, having led a variety of organisations across the charitable and public housing sectors. She is Chief Executive Officer of Hanover Housing Association, having previously been Chief Executive of Action for Children. In 2014 she became Chair of the Early Intervention Foundation. Dame Clare qualified as a social worker at Bristol University in 1984 and worked for social care and housing organisations including Centrepont, and Stonham Housing Association. She was also a commissioner on the Royal Society of Arts (RSA) 2020 Commission into Public Services; and former Board Member of The Guinness Partnership. She is a Fellow of the RSA, and Chair of the Community and Voluntary Services Honours Committee. From 2011 until 2013 she

chaired the Commission on the Future of Hospice Care. She was appointed as non-executive member of the Board on 10 January 2018 by the Public Accounts Commission for a three-year term of office, renewable for a second and final three-year term.

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## The NAO Board and Leadership Team



Max Tse joined the NAO in 2011. For five years he led the NAO's value-for-money audit of the Department for Work & Pensions, and more recently has been responsible for the NAO's approach to digital transformation in government. Max is now the Executive Leader with oversight of Digital Transformation.

Prior to joining the NAO, Max worked as a consultant with McKinsey & Co. He has worked in the UK and overseas in a range of sectors, including logistics, regulatory strategy, retail, climate finance and health.



Michael Whitehouse OBE was appointed Chief Operating Officer in July 2009. Michael has extensive experience of value-for-money work across government and internationally and is a qualified accountant. Prior to retiring in April 2017, Michael was responsible for the strategy, capability and operational performance of the NAO, and led the NAO's work on cross-government issues. Michael was also chair of the Operational Capability Committee.

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**7** The Board is supported by two committees, both of which consist solely of non-executive members.

#### Audit Committee

The Committee supports the Board by reviewing our internal controls, risk management processes and governance arrangements, as well as the quality and reliability of our financial reporting. It also considers the external auditor's annual value-for-money report on the NAO.

#### Remuneration and Nominations Committee

The Committee determines the framework for remunerating the executive members of the Board. It also oversees any major changes in employee benefits. The Committee also advises the Chair and the C&AG on succession planning for the Leadership Team and Board.

**8** There is a clear division of responsibility between the Chair and the C&AG. The Chair is responsible for leading, and effective working of, the Board. The C&AG is responsible for implementing the strategy, making audit judgements, deciding a programme of wider assurance work and reporting the results of this work to Parliament.

**9** Each year the C&AG and Board agree the NAO Strategy and the annual budget (Estimate), which are submitted to the Public Accounts Commission for consideration and approval. The Board and C&AG also prepare an Annual Report and Accounts. The Board must also recommend the NAO's external auditor for appointment by the Public Accounts Commission.



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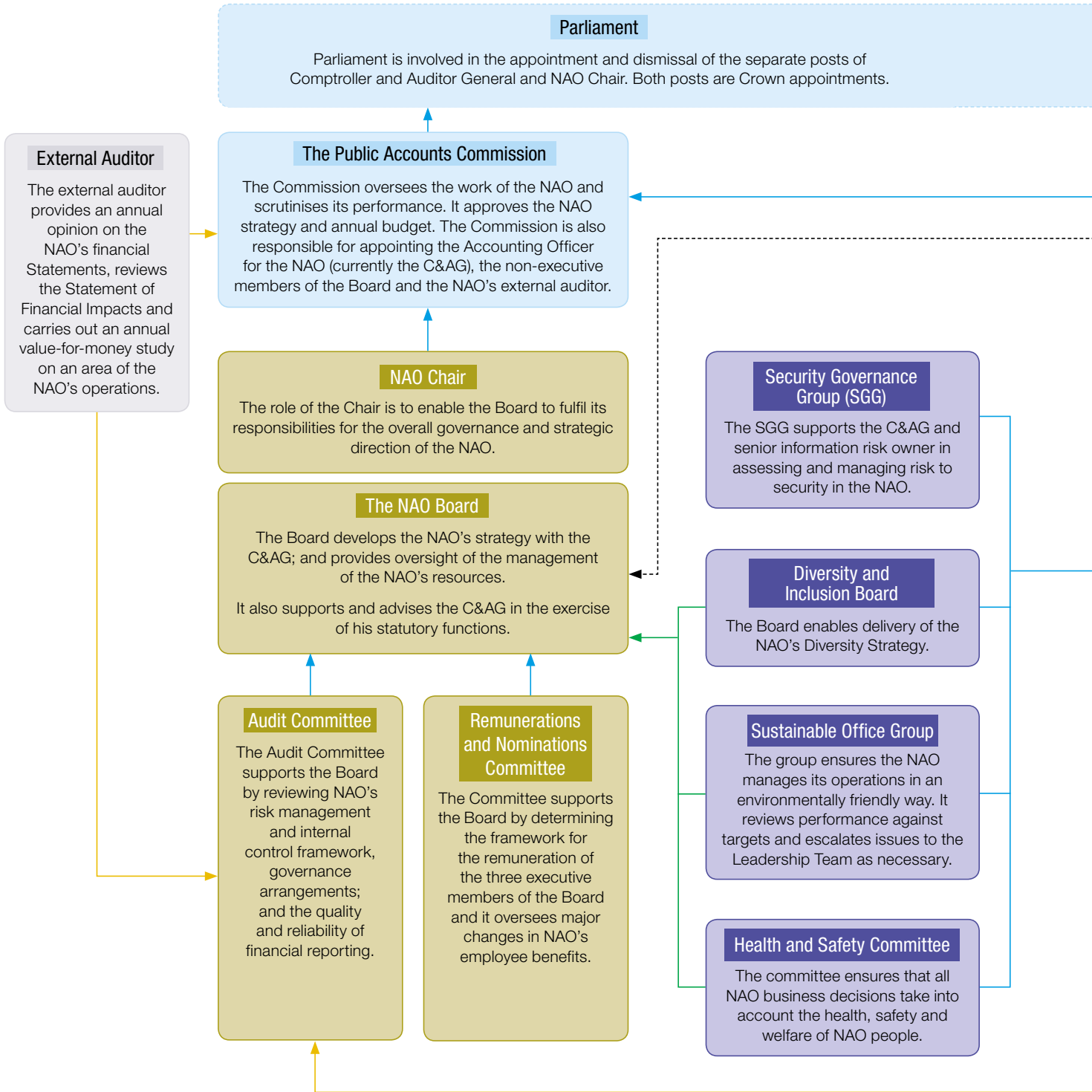
**10** The Board is responsible for the programme of work undertaken outside of the C&AG's statutory responsibilities. This programme of work includes those financial audits undertaken under the Companies Act 2006, the value-for-money review of the BBC, and our work with international organisations. It approves this programme of work and the resources required annually.

**11** The Board met formally seven times during 2017-18, in addition to a strategy day, to focus on progress against strategy and discuss future scenarios for the way public services are delivered. The Board also undertook an externally facilitated review of its performance. The review concluded the Board should move to a more strategic way of working, which it is implementing. The Chair has evaluated the performance of the non-executive members and the Chair's performance has been evaluated by the senior independent director.

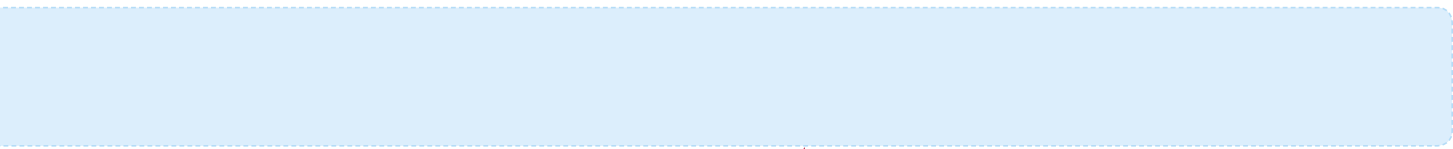
**12** The C&AG is supported in his role by the Leadership Team, who helps the C&AG to develop and implement strategy, lead staff, set work priorities, monitor performance and manage risk. From 1 April 2018, the C&AG expanded the Leadership Team from five to seven members to provide for greater capacity for the team to be directly involved with assignments where appropriate.

**13** Our formal governance structure during 2017-18 is as follows overleaf:

# NAO governance framework



Source: National Audit Office



**Comptroller and Auditor General (C&AG)**

The role of the C&AG is to support Parliament in holding government to account for spending public money. He is the chief executive officer of the NAO, and supported by the NAO in discharging his role.

The C&AG is also Accounting Officer of the NAO, appointed to this position by the Public Accounts Commission to whom in this role he reports.

**Internal Audit**

The internal auditor provides an independent assurance and advisory function to the C&AG, in his capacity as Accounting Officer, and to the Audit Committee.

**Leadership Team**

The Leadership Team supports the C&AG in the exercise of his statutory duties. The Leadership Team provides executive management and governance to the operations and delivery of the NAO. Within this team is the security information risk owner.

**Operational Capability Committee (OCC)**

The OCC supports the Leadership Team to deliver appropriate resources to enable the NAO to achieve its strategic objectives. Drives continuous improvement in NAO processes.

**Change Management and Assurance Committee (CMAC)**

The CMAC supports the Leadership Team by overseeing the change portfolio, thereby ensuring change is properly prioritised and aligned.

**Value For Money (VfM) Quality Committee**

The committee advises the Leadership Team on all aspects of quality relating to the NAO's value-for-money and investigations work, including oversight.

**Financial Audit Director Group (FADG)**

FADG advises the Leadership Team on all aspects of quality relating to the NAO's financial audit work, including oversight.

**Key**

○ Parliament and Public Accounts Commission	→ Reporting
○ Parliament's independent statutory auditor	→ Accountability
○ Independent assurance	→ Code of practice dealing with the relationship between the NAO and C&AG
○ Executive management	→ Assurance
○ Statutory governance	→ Information

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## Review of effectiveness

**14** The C&AG's review of effectiveness of the system of internal control is informed by the work of the Director of Internal Audit and Assurance (DIAA), the executive leaders within the NAO who have responsibility for the development and maintenance of the internal control framework, comments made by the external auditors in their management letter and other reports.

**15** In his 2017-18 annual report to the C&AG, the DIAA concludes: "The NAO has adequate and effective governance, risk and control arrangements." DIAA has arrived at his opinion through:

- conducting a detailed risk-based internal audit needs assessment, from which he has prioritised activity over a three-year planning horizon to design an internal audit strategy and annual operational plan;
- updating NAO's three lines of defence model, which is aligned to NAO's corporate risk register to provide a 'bird's eye view' of the assurance framework;
- designing and applying a risk-based methodology, which has been validated by an External Quality Assessment commissioned by the Audit Committee as conforming to the Public Sector Internal Audit Standards;
- delivering 28 individual assurance assignments and advisory reports during the year and, where appropriate, agreeing an action plan with system owners to secure improvements; and
- monitoring the implementation of internal audit recommendations throughout the year and assessing progress as 'good'.

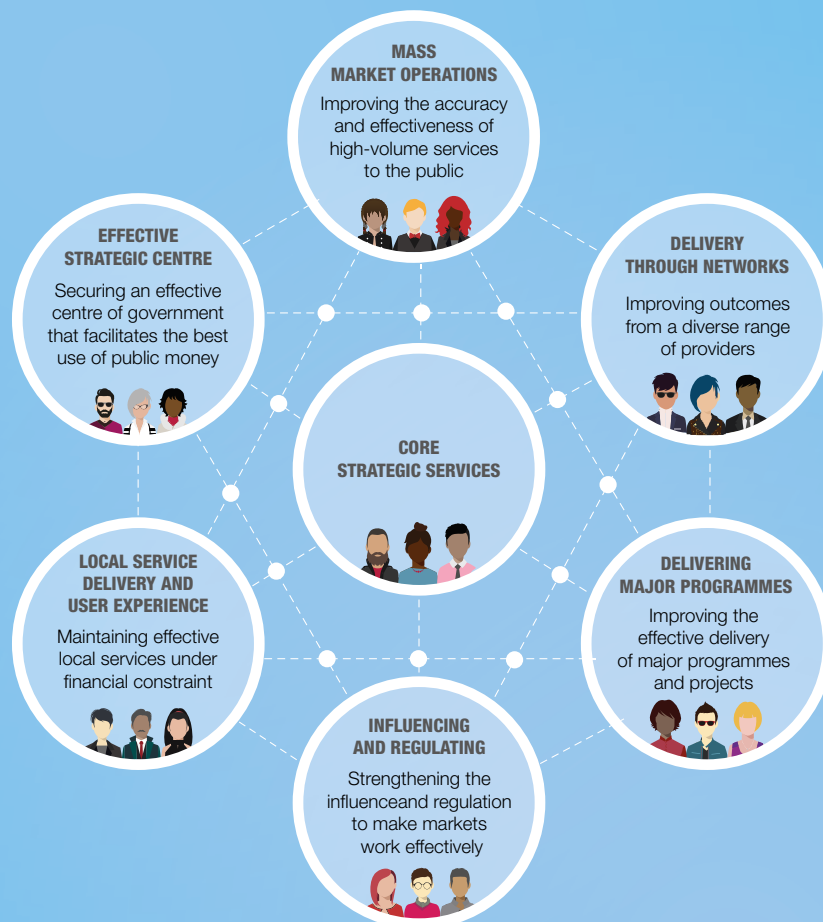
**16** The C&AG is able to report that there were no significant weaknesses in the NAO's system of internal controls in 2017-18 that affected the achievements of the NAO's key policies, aims and objectives.

## Structure

**17** Our strategy is to use the insights we derive as the government's external auditors to help improve public services. We structure our audit teams into six groups, known as clusters. Each cluster covers government departments facing similar strategic issues, such as major infrastructure projects and programmes or local service delivery. By focusing our resources on the strategic issues shared between departments, we can concentrate our efforts on the challenges likely to have the most significant beneficial effect on public services. This maximises our ability to share knowledge across audit teams and builds subject matter expertise. It also enables us to carry out comparative analysis and encourages collaborative working.

**18** The NAO is supported by a central 'Core Strategic Services' cluster, which provides strategic input to the Leadership Team and expert advice on the quality of our work and the value we deliver to audited bodies and Parliament. This central cluster also ensures our internal operations run smoothly, our funds are used cost-effectively and our work and the insights from it are communicated widely to help drive public service improvement.

## Our clusters and their objectives



Our clusters are supported by six networks of experts

- 1 Commercial and Contracting;
- 2 Corporate Finance;
- 3 Digital;
- 4 Operations and Process Management;
- 5 Project and Programme Management Delivery; and
- 6 Methods, Economics and Statistics.

## People

**19** We publish an organisation chart showing our structure and leaderships' responsibilities on our website, available at: [www.nao.org.uk/about-us/our-work/governance-of-the-nao/](http://www.nao.org.uk/about-us/our-work/governance-of-the-nao/).

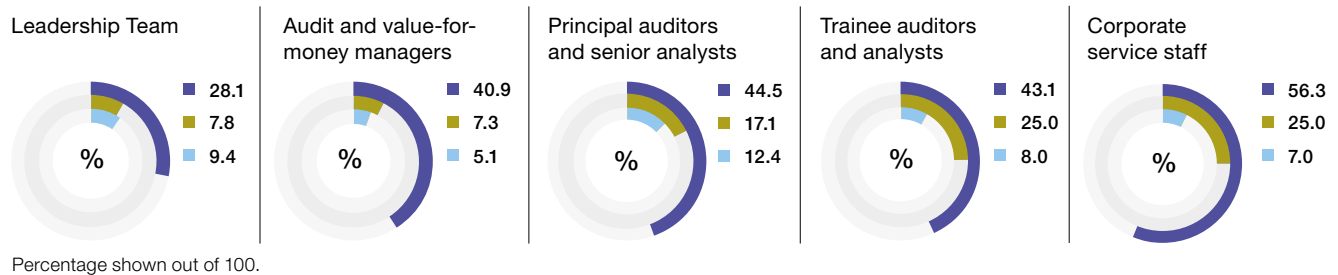
**20** Staff composition as 31 March 2018 is set out in the figure below. The following figure sets out the staff distribution by grade and diversity for all staff in post (as opposed to full-time equivalent).

### Average number of persons employed

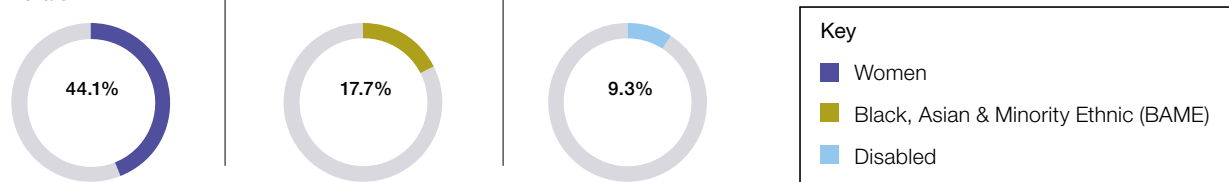
	2017-18	2016-17	2015-16
Full-time equivalent permanent staff	806	803	796
Inward secondees	3	3	5
Temporary staff	5	5	9
<b>Total</b>	<b>814</b>	<b>811</b>	<b>810</b>

### Staff composition as at 31 March 2018

#### Grade diversity as at 31 March 2018



#### Totals



Data are expressed as a percentage of total population including staff who have not declared or selected 'prefer not to say'.

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**21** As at 31 March 2018 the proportion of women above manager level was 28%, a figure that has not shifted significantly over the past three years. This is impacted by historically fewer female applicants for promotion from the feeder grade, and is an area we must focus our efforts on going forward. The gender balance in more junior grades is healthier, although we have faced challenges in consistently achieving a 50:50 ratio of women to men joining our graduate programme in recent years. We have taken a proactive approach as part of the current graduate recruitment campaign by encouraging female applicants to pursue their application through the NAO selection process, to help secure a more balanced intake. We also commissioned an external review of our trainee selection processes in March 2018 to identify further actions we can take to widen further the diversity of our intake.

**22** Over the past three years representation of Black, Asian and Minority Ethnic (BAME) colleagues has also remained static, at 18% of the workforce. We have made some progress in increasing BAME representation in our annual graduate intake and, currently, BAME staff make up more than 25% of the trainee population. However, the proportion of BAME staff above manager level remains low. We are determined to improve the diversity of our manager cadre and will take specific actions to improve BAME representation at manager level as part of our new diversity and inclusion strategy.

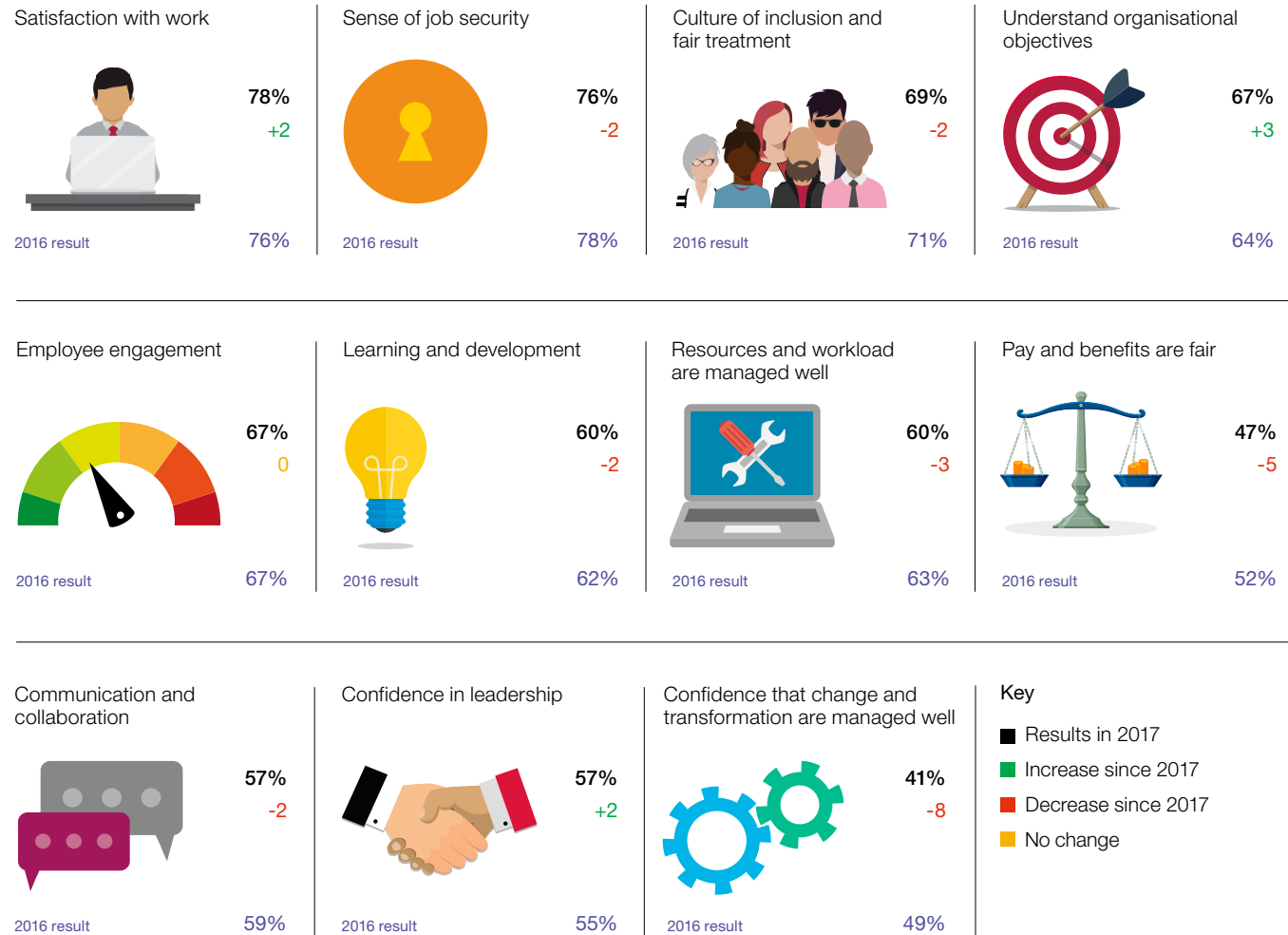
#### Staff survey

**23** We conduct an annual survey of our people and benchmark the results against comparable organisations. In 2017, 78% of NAO staff completed the annual survey, which was the same percentage as 2016. We are pleased that the results largely show a consolidation of the significant increases in our 2016 survey, and that they continue to compare favourably with our benchmarks.

**24** Employee engagement, at 15% higher than the civil service average, reflects the pride our people feel in working at the NAO and their motivation. Although we are pleased to maintain our positive level of engagement, we want to see further improvements in how our people feel about working at the NAO. Our key areas of focus in the coming year will be: to further improve our internal communications, particularly how we consult with our people; to be clearer about the changes we are making within the organisation and why we are making them; and to develop our workforce planning capability to improve our peak workload management.

## National Audit Office people survey results

### Results of the survey in 2017 compared with 2016



#### Note

- 1 Each year the NAO conducts a people survey to understand staff opinions on a range of work-related issues. This table presents a top-level summary against the categories used. The percentages show the level of positive responses. In total there are 75 questions in the survey, the results of which are summarised in the 11 topic areas listed above.



## Financial information

**25** Each year, the NAO's external auditor undertakes an annual value-for-money review of a specific aspect of the NAO's business. In 2017 the topic for review was *Delivery of benefits from the NAO's IT-enabled change programme*. The conclusion the external auditor has drawn is overall positive. The review makes 13 recommendations for improvement, which management is taking forward.

**26** The report was submitted to the Public Accounts Commission in December 2017 and can be found on the Commission's website, available at: [www.parliament.uk/documents/public-accounts-commission/15-NAO-VFM-report-on-IT-enabled-change-programme.pdf](http://www.parliament.uk/documents/public-accounts-commission/15-NAO-VFM-report-on-IT-enabled-change-programme.pdf).

**27** Our full financial information is contained in our Annual Report and Accounts 2017-18, which can be found on our website, available at: [www.nao.org.uk/report/nao-annual-report-and-accounts-2017-18](http://www.nao.org.uk/report/nao-annual-report-and-accounts-2017-18). The table below sets out our expenditure and income under six operating segments. As would be expected from the nature of our work, the largest segment of expenditure relates to statutory financial audit, which represents 65% of NAO's gross expenditure. The remainder relates to other assurance work. The C&AG's functions is reported as a separate segment.

	2017-18								
	Audit and assurance	Value for money	Investigations and insight	Support to Parliament	International relations	Comptroller function	Voted	Non-voted	Total
	£000	£000	£000	£000	£000	£000	£000	£000	£000
Gross expenditure	54,417	13,339	10,392	4,432	1,212	113	<b>83,905</b>	294	<b>84,199</b>
Income from services provided	(16,375)	–	–	(401)	(508)	–	<b>(17,284)</b>	–	<b>(17,284)</b>
Rental income	(1,199)	(294)	(229)	(98)	(27)	(2)	<b>(1,849)</b>	–	<b>(1,849)</b>
<b>Net expenditure</b>	<b>36,843</b>	<b>13,045</b>	<b>10,163</b>	<b>3,933</b>	<b>677</b>	<b>111</b>	<b>64,772</b>	<b>294</b>	<b>65,066</b>

The NAO reports expenditure and income under six operating segments, descriptions of which can be found on page 19 to 20 of the Annual Report. Non-voted expenditure includes the C&AG's and Chair's salaries and is paid directly from the Consolidated Fund, which is outside of the control of the NAO.

Income from services includes fees charged on UK and international audits, costs recovered on the NAO's outward secondment programme to support Parliament and other government bodies, and fees charged for some of the NAO's international relations and overseas capacity-building work. Rental income cannot be directly attributed to the NAO's operating segments and has been apportioned in line with gross expenditure.

We consider the chief operating decision body of the NAO to be the Leadership Team, details of its membership can be found on pages 56 to 61 of the Annual Report. Due to the nature of the NAO's activities, the Leadership Team does not receive assets and liabilities analysed by operating segment and therefore such an analysis is not presented here.

	2016-17							Voted	Non-voted	Total
	Audit and assurance	Value for money	Investigations and insight	Support to Parliament	International relations	Comptroller function				
	£000	£000	£000	£000	£000	£000	£000			
Gross expenditure	50,468	16,102	9,912	5,079	1,362	155	<b>83,078</b>	291	<b>83,369</b>	
Income from services provided	(16,321)	–	–	(568)	(476)	–	<b>(17,365)</b>	–	<b>(17,365)</b>	
Rental income	(1,083)	(345)	(213)	(109)	(29)	(3)	<b>(1,782)</b>	–	<b>(1,782)</b>	
<b>Net expenditure</b>	<b>33,064</b>	<b>15,757</b>	<b>9,699</b>	<b>4,402</b>	<b>857</b>	<b>152</b>	<b>63,931</b>	<b>291</b>	<b>64,222</b>	

**28** Our Annual Report contains a detailed remuneration report. We also publish details of senior staff remuneration and Leadership Team and Board members' travel and subsistence costs and hospitality they provided and received. Details can be found on our website, available at: [www.nao.org.uk/about-us/our-work/governance-of-the-nao/transparency/](http://www.nao.org.uk/about-us/our-work/governance-of-the-nao/transparency/).

**29** We are independent of government pay policy, although we take HM Treasury guidance and the wider public sector pay environment into account in considering our own approach to pay. Performance-related increases focus solely on base pay and there is no system of bonuses. In addition to salary, the largest non-pay benefit (along with our investment in training) is the civil service pension scheme.

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# Appendix Two

## ASSURANCE AND CONTROL

### Financial audit

- 1** Most of the Comptroller and Auditor General's (C&AG's) audits are by statutory appointment, so he cannot withdraw or decline them. However, the C&AG can report to Parliament on matters that might otherwise have caused him to withdraw from the engagement. No such instances arose during 2017-18.
- 2** Where the C&AG is appointed as auditor other than by statutory appointment, he must be confident that the terms and scope of the work are appropriate and that there are adequate resources. He has sole responsibility for audit judgements and conclusions reached, including the right to decline or withdraw from any of these engagements. He is advised by the relevant engagement director and the Director of Financial Audit Practice and Quality in engagement acceptance matters.
- 3** Each year the risks associated with an audit will change and therefore we keep appointments under review. Each year teams consider the integrity and competence of the client's board members and senior managers as well as the specific audit team's competence and any specialist requirements to support the engagement. Our procedures are designed to ensure that the team meets the ethical and professional requirements that we and the auditing profession stipulate.

### Policies and procedures

- 4** The Director of Financial Audit Practice and Quality issues the *Financial Audit Manual*, and this is the main reference source for audit policy and guidance. It sets out the requirements of International Standards on Auditing (ISAs) (UK) and how we must apply these. The manual is updated regularly, to incorporate any changes to professional standards and internal policy changes, which the Leadership Team agrees.
- 5** Our audit methodology, as set out in the *Financial Audit Manual*, is integrated with the software package we use to document audit work. The software and other tools and templates make it straightforward for engagement teams to comply with standards and internal policy. They also encourage efficient working by increasing standardisation and reducing the need for teams to recreate standard audit approaches. The audit approach is codified in centrally defined work programmes with customisation requiring central approval.

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## Control framework

**6** Overall responsibility for a financial audit rests with the engagement director. We use a two-stage internal review process for audits to ensure the quality of financial audit work:

### First stage review

A senior member of the engagement team reviews all audit tests and supporting working papers, focusing on audit quality.

### Second stage review

The engagement director performs a second review to confirm that sufficient and appropriate evidence has been obtained to support the recommended audit opinion. This review focuses on the risks of material misstatement and key judgements made by the engagement team.

**7** Where an engagement director identifies a matter that involves significant professional judgement they must consult the Practice and Quality Team, which is led by the Director of Financial Audit Practice and Quality, before concluding on that matter.

**8** The most significant technical issues will be considered by an audit panel. Panels are convened to enable audit teams to consult on specific issues as these arise. The panel will include representatives from the Leadership Team, the Director of Financial Audit Practice and Quality, and senior engagement team members. The panel may also include the Engagement Quality Control Reviewer (EQCR) and any other experienced senior National Audit Office (NAO) staff the director considers appropriate.

**9** The EQCR is an experienced financial audit director independent from the engagement team, or a panel of such individuals who may be assigned to an engagement. The EQCR's role is primarily to challenge key audit judgements and review evidence supporting the engagement team's conclusions on significant matters. EQCRs are assigned to most audits where a qualification of the audit opinion seems likely or where the audit risk is particularly high.

**10** Our internal Compliance and Quality Unit reviews the files of certain audits (mainly those that are high risk) at the planning stage and before the audit report is issued (hot reviews). These reviews focus on compliance with key areas of our financial audit process.

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**11** The Compliance and Quality Unit also reviews the audit files of a sample of completed audits each year (cold reviews). The process covers all categories of audits and the full range of our clients. The reviews are completed by experienced audit managers. Their purpose is to assess:

- the audit's compliance with professional standards and our audit policy, including reviewing the planned response and work completed to address the main risks;
- the quality of evidence the team collected to support the main audit risks; and
- any opportunities to improve documentation and make efficiencies in the audit approach for the following audit cycle.

### Audit licences

**12** Individuals supervising, managing or directing a financial audit will usually hold the relevant audit licence. The Director of Financial Audit Practice and Quality usually grants audit licences to all staff who:

- are Consultative Committee of Accounting Bodies (CCAB)-qualified or exam-qualified;
- have an appropriate level of recent financial audit experience;
- have an appropriate level of Continuous Professional Development in the previous year; and
- have signed the NAO's Code of Conduct.

**13** The Director of Financial Audit Practice and Quality oversees the arrangements for allocating licences to staff whose work involves complex IT systems, the audit of companies, pension schemes, charities and accounts prepared under International Public Sector Accounting Standards. All staff holding a specialist licence must also hold a general audit licence, have an appropriate level of recent experience in the specialist area and have attended relevant technical updates.

**14** Members of staff who do not hold the appropriate licence can hold senior roles within the engagement team, provided supervision arrangements are put in place. For example, a pension scheme audit where neither the engagement director nor engagement manager holds a pensions licence will be assigned a second director who does hold a pensions licence. The engagement director must consult with the second director at regular points during the audit, and before issuing the audit report.

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## Value-for-money and investigations

**15** The NAO's standards for value-for-money and other non-financial audit work (VfM standards) set out the expectations that all value-for-money studies, investigations and other major non-financial audit outputs must meet. Colleagues working on non-financial audits are expected to adhere to the standards and this is considered as part of the internal quality assurance arrangements. There are twelve standards covering:

- integrity, objectivity and independence;
- work proposal and selection;
- design and planning;
- evidence and analysis;
- forming conclusions and recommendations;
- reporting;
- quality assurance;
- project management and monitoring;
- engagement with audited bodies;
- engagement with other stakeholders;
- achieving impact; and
- learning lessons and sharing knowledge.

**16** The standards for VfM are underpinned by core policies and procedures which describe our approach to this strand of work, which is to provide independent analysis and assurance to Parliament on how public money has been spent and make recommendations that lead directly to service improvements. The policies are supplemented by detailed guidance relating to specific stages in the lifecycle of a value-for-money study, investigation, and/or other type of non-financial audit including analytical and technical methods and approaches. The guidance is held electronically and updated as and when is required.

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## Control framework

**17** Directors ensure that there are proportionate and appropriate quality assurance arrangements for their studies and investigations. We assign a partner director and case manager. The partner director acts as a constructive critic and the case manager is available to provide technical and practical advice and guidance throughout the audit. Quality is controlled using the following mandatory framework:

- Study and product selection: the C&AG and leadership team select value-for-money studies/investigations after information gathering, proposal development and review, to ensure proposals will have impact and fit with our strategic objectives and Parliament's needs.
- Approving the study concept: the C&AG examines and approves a study concept, considering the rationale, scope, product type and strategic fit of the proposed piece of audit work
- Budget approval and confirming quality arrangements: clusters scrutinise and approve quality assurance arrangement and budgets after the C&AG has agreed the scope of the audit work.
- Proof-of-concept meeting: when most of the fieldwork has been completed, the C&AG challenges the audit team on how the evidence collected supports the logic of the intended report.
- C&AG review: the C&AG reviews the draft provisional audit findings and the draft final report. Once he is content the team sends the draft to the audited body for consideration and comment.
- Copy editor and data presentation review: the copy editor edits the draft report before publication. This is designed to confirm adherence to our publication standards and readability.
- Optional quality assurance: a range of additional quality assurance is available for teams, including reviews of the draft report, methods-specific quality assurance, and external advice or consultancy.
- Post-project review. After we publish the report, the study team reviews the conduct of the study/investigation to identify examples of good practice and lessons learned, which they disseminate across the organisation.
- Internal cold review: we review about 12 publications each year, from across the NAO and from our full range of wider assurance products. We identify (using a standard set of criteria) and examine any risks to quality or compliance, or both, with the VfM standards. Eleven outputs published in 2017-18 have been subject to an internal cold review. The reviews highlighted some common issues including: consistency in documenting audit evidence; and compliance with mandatory steps for documenting director review.

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- External cold review: a sample of published value-for-money reports (12 in 2017-18) are subject to an independent, external review. The reviewer considers the report against a set of agreed criteria.

## External monitoring

### External review – financial audit

**18** The Audit Quality Review team (AQRT) of the Financial Reporting Council reviews a selection of audit files. In 2017-18, the AQRT reviewed seven completed audit files (2016-17: six), of which four (2016-17: two) were performed under the Companies Act 2006. At the time of publication of this Transparency Report the AQRT review is still in progress. We have already started to respond to their initial findings and develop a plan to monitor the progress of agreed actions. We have communicated the findings to all staff and held more detailed discussions with directors and managers in group meetings.

**19** The AQRT also carried out a cyclical review of the NAO's processes, policies and procedures supporting audit quality, including a review of internal quality monitoring and consultative and engagement quality review (EQCR) arrangements and a follow-up review of prior year findings.

**20** The inspection highlighted some areas for further improvement while also reflecting on the improvements we had already put in place. The issues, which are subject to finalisation, are expected to include the need for the NAO to continue to build on the progress that it has made in response to previous findings.

**21** We took a number of actions in 2017-18 to respond to the findings from the AQRT review in 2016-17 that are now embedded in our audit methodology. We:

- communicated the AQRT's findings to all staff and incorporated the feedback into our annual assurance training;
- held detailed discussions of AQRT findings with directors and managers in group meetings;
- enhanced our mandatory consultation procedures for our highest-risk audits;
- updated our standard audit documentation templates and guidance including our *Financial Audit Manual*;
- developed enhanced management information to monitor financial audit quality covering client delivery risk, critical path management, audit risk and staffing;
- provided mandatory training to all EQCR directors to ensure that they adopt a consistent approach in undertaking and documenting their role;



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- re-emphasised the importance of embedding our consideration of risk throughout the audit via office-wide annual technical updates;
  - provided additional training for engagement managers and engagement directors where they are adopting that role for the first time; and
  - committed to strengthening the capacity of our Compliance and Quality Unit and we redesigned the internal review programme.

**22** We are continuing to invest in our capability to do digital audits, both with increased technical training for our IT Audit specialists, and by training a group of financial audit staff on IT audit fundamentals to allow them to also undertake supervised IT audit work. We have created a specialist data analytics team, allowing us to build our skills in this area and to make increased use of data analytics in our financial audit work.

### **External review – value-for-money and investigation reports**

**23** For more than two decades we have used external specialists to review value-for-money reports. In 2017-18, a sample of 12 reports were reviewed by independent experts from Oxford Business Schools, Risk Solutions and RAND Europe.

Our reviewers assess the report against a set of criteria:

- scope;
- qualitative analysis;
- structure and presentation;
- graphics and statistics;
- appropriateness and use of methods;
- synthesis of conclusions, recommendations (where made), systemic issues; and
- overall perception.

**24** They provide a written review assessing how each report performs against the criteria in paragraph 23 above, including an overall assessment. The VfM Quality Group uses these reviews as the basis of discussions on quality.

**25** Our central Practice and Quality Team also seeks formal feedback from clients on individual studies, including the conduct of the study team, whether the study was of high technical quality, our staff's professionalism, engagement with the client, and the team's knowledge. Our surveys are conducted electronically and are sent to the appropriate senior working-level contacts for each report at the audited body. This gives us better and more timely feedback.

# Appendix Three

## TRANSPARENCY REPORT DISCLOSURE REQUIREMENTS

1 The table below shows where the disclosures required by The Statutory Auditors (Transparency) Instrument 2008 can be found in this Transparency Report.

Provision of the Instrument	How the National Audit Office complies with the Instrument
A description of the legal structure and ownership of the transparency reporting auditor.	See Appendix One: Governance and accountability.
Where the transparency reporting auditor belongs to a network, a description of the network and the legal and structural arrangements of the network.	Not applicable to the National Audit Office (NAO).
A description of the governance structure of the transparency reporting auditor.	See Appendix One: Governance and accountability.
A description of the internal quality control system of the transparency reporting auditor and a statement by the administrative or management body on the effectiveness of its functioning.	See Part Two for the internal quality control system and Appendix Two: Assurance and control. As described in this report, our internal quality control system is made up of many different processes and reviews. Drawing on our ongoing analysis of all aspects of the system in place gives us reasonable assurance that our internal quality control system is functioning effectively.
A statement of when the last monitoring of the performance by the transparency reporting auditor of statutory audit functions within the meaning of paragraph 13 of Schedule 10 to the Act (as amended by regulation 23 of the Statutory Auditors and Third Country Auditors Regulations 2007 (S.I. 2007/3494) took place.	A review of our statutory audit performance was ongoing at the time of publication. We have set out some details of this review in Part Two, Audit independence and quality and Appendix Two: Assurance and control, External Monitoring sections.
A list of public interest entities in respect of which an audit report has been made by the transparency reporting auditor in the financial year of the auditor; and any such list may be made available elsewhere on the website specified in regulation 4 provided that a clear link is established between the transparency report and such a list.	In 2017-18, the NAO audited five public interest entities: <ol style="list-style-type: none"><li>1. Network Rail Infrastructure Finance PLC</li><li>2. CTRL Section 1 Finance PLC</li><li>3. LCR Finance PLC</li><li>4. Northern Rock Asset Management Limited</li><li>5. HM Treasury UK Sovereign SUKUK PLC</li></ol>
A description of the transparency reporting auditor's independence procedures and practices including a confirmation that an internal review of independence practices has been conducted.	See Part Two, Independence section for details of our independence procedures. Consideration of our independence practices is completed throughout the year. We can therefore confirm that an internal review of our practices has been conducted in 2017-18.
A statement on the policies and practices of the transparency reporting auditor designed to ensure that persons eligible for appointment as a statutory auditor continue to maintain their theoretical knowledge, professional skills and values at a sufficiently high level.	The NAO's policies and practices are designed to ensure that our staff continue to maintain their theoretical knowledge, professional skills and values at a sufficiently high level. See Part Two, Our People section for further detail of these policies and practices.
Financial information for the financial year of the transparency reporting auditor to which the report relates, including the showing of the importance of the transparency reporting auditor's statutory audit work.	See Appendix One: Financial Information section.
Information about the basis for the remuneration of partners.	See Appendix One: Governance and accountability.

# Appendix Four

## REVIEW OF NAO COMPLIANCE WITH THE AUDIT FIRM GOVERNANCE CODE 2016-17

- 1 We are not required to comply with the Audit Firm Governance Code as compliance is required for those firms having 20 or more listed entities as clients. However, in the spirit of adhering to best practice, to the extent that the Code is relevant to the National Audit Office (NAO), which is a Supreme Audit Institution, we set out how we comply with the Audit Firm Governance Code.
- 2 Throughout the code reference to 'a firm' means a firm that audits listed companies in the UK.

	Provision of the code	How the NAO complies with the code
<b>A – Leadership</b>	A.1: Owner accountability principle – The management of a firm should be accountable to the firm’s owners and no individual should have unfettered powers of decision.	The owner accountability principle does not directly apply to the NAO. The Comptroller and Auditor General (C&AG) has statutory powers given by Parliament.
	A.1.1: The firm should establish Board or other governance structures, with matters specifically reserved for their decision, to oversee the activities of the management team.	All other provisions are covered by Appendix One: Governance and accountability and relevant sections of our Annual Report and Accounts.
	A.1.2: The firm should state in its transparency report how its governance structures and management team operate, their duties and the types of decisions they take.	
	A.1.3: The firm should state in its transparency report the names and job titles of all members of the firm’s governance structures and its management team, how they are elected or appointed and their terms, length of service, meeting attendance in the year and relevant biographical details.	
	A.1.4: The firm’s governance structures and management team and their members should be subject to formal, rigorous and ongoing performance evaluation and, at regular intervals, members should be subject to re-election or re-selection.	
	A.2: Management principle – A firm should have effective management which has responsibility and clear authority for running the firm.	These provisions are set out in the Budget Responsibility and National Audit Act 2011, which we fully comply with.
	A.2.1: The management team should have terms of reference that include clear authority over the whole firm, including its non-audit businesses and these should be disclosed on the firm’s website.	The management team’s terms of reference are set out in the NAO’s Annual Report and in this Transparency Report, available on our website.
<b>B – Values</b>	B.1: Professionalism principle – A firm should perform quality work by exercising judgement and upholding values of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour in a way that properly takes the public interest into consideration.	These provisions are covered by our Code of Conduct and NAO corporate reporting, available on our website.

B.1.1: The firm's governance structures and management team should set an appropriate tone at the top through its policies and practices and by publicly committing themselves and the whole firm to quality work, the public interest and professional judgement and values.

This provision is covered by our Code of Conduct and NAO corporate reporting, including this Transparency Report, available on our website.

B.1.2: The firm should have a Code of Conduct which it discloses on its website and requires everyone in the firm to apply.

All NAO people, including the non-executive members of the Board, complete a Code of Conduct return annually. Confirmation of this is contained in this Transparency Report which is published on our website.

B.2: Governance principle – A firm should publicly commit itself to this Audit Firm Governance Code.

We are not required to comply with the Audit Firm Governance Code, however, in the spirit of adhering to best practice, to the extent that the Code is relevant to the NAO, which is a Supreme Audit Institution, we set out how we comply with the Audit Firm Governance Code in this Transparency Report.

B.2.1: The firm should incorporate the principles of this Audit Firm Governance Code into an internal Code of Conduct.

The NAO's Code of Conduct, which is approved by the Board, sets out the NAO's framework of professional and ethical behaviour.

B.3: Openness principle – A firm should maintain a culture of openness which encourages people to consult and share problems, knowledge and experience in order to achieve quality work in a way that properly takes the public interest into consideration.

This provision is addressed through our values and strategy, details of which can be found in our Annual Report and the NAO Strategy document, including this Transparency Report, published on our website.

## C – Independent non-executives

C.1: Involvement of independent non-executives principle – A firm should appoint independent non-executives who through their involvement collectively enhance shareholder confidence in the public interest aspects of the firm's decision-making, stakeholder dialogue and management of reputational risks including those in the firm's businesses that are not otherwise effectively addressed by regulation.

These provisions are set out in the Budget Responsibility and National Audit Act 2011, which we fully comply with.

C.1.1: Independent non-executives should: have the majority on a body that oversees public interest matters; and/or be members of other relevant governance structures within the firm. They should also meet as a separate group to discuss matters relating to their remit.

This provision does not apply to the NAO in view of the C&AG's statutory independence as set out in the Budget Responsibility and National Audit Act, 2011.

C.1.2: The firm should disclose on its website information about the appointment, retirement and resignation of independent non-executives, their duties and the arrangements by which they discharge those duties and the obligations of the firm to support them. The firm should also disclose on its website the terms of reference and composition of any governance structures whose membership includes independent non-executives.

These provisions are set out in the NAO's Annual Report and Accounts which is published on our website. The terms of reference of the NAO Board and the two committees that report to the Board (the Audit Committee and the Remuneration and Nominations Committee) are disclosed on our website.

C.2: Characteristics of independent non-executives principle – The independent non-executives' duty of care is to the firm. They should command the respect of the firm's owners and collectively enhance shareholder confidence by virtue of their independence, number, stature, experience and expertise.

These provisions are set out in the Budget Responsibility and National Audit Act 2011, which we fully comply with.

C.2.1: The firm should state in its transparency report its criteria for assessing the impact of independent non-executives on the firm's independence as auditors and their independence from the firm and its owners.

Not applicable to the NAO because of NAO's unique statutory position.

<p>C.3: Rights of independent non-executives principle – Independent non-executives of a firm should have rights consistent with their role, including a right of access to relevant information and people to the extent permitted by law or regulation, and a right to report a fundamental disagreement regarding the firm to its owners and, where ultimately this cannot be resolved and the independent non-executive resigns, to report this resignation publicly.</p>	<p>These provisions are set out in the Budget Responsibility and National Audit Act 2011, which we fully comply with.</p>
<p>C.3.1: Each independent non-executive should have a contract for services setting out their rights and duties.</p>	<p>We comply fully with this provision.</p>
<p>C.3.2: The firm should ensure that appropriate indemnity insurance is in place in respect of legal action against any independent non-executive.</p>	<p>Indemnification of independent non-executives is covered by the Budget Responsibility and National Audit Act 2011.</p>
<p>C.3.3: The firm should provide each independent non-executive with sufficient resources to undertake their duties including having access to independent professional advice at the firm's expense where an independent non-executive judges such advice necessary to discharge their duties.</p>	<p>We provide sufficient resources to the independent non-executives to undertake their duties.</p>
<p>C.3.4: The firm should establish, and disclose on its website, procedures for dealing with any fundamental disagreement that cannot otherwise be resolved between the independent non-executives and members of the firm's management team and/or governance structures.</p>	<p>Included in the Senior Independent Director's role is their duty to act as a mediator between independent non-executives and management.</p> <p>In the event of any fundamental disagreement between the independent non-executive members and NAO management, resolution would be sought through discussion by the NAO Board. In the unlikely event that the issue remained unresolved, it would be for the C&amp;AG to determine the most appropriate course of action consistent with his independent statutory role and status. We make this disclosure in this Transparency Report which is published on our website.</p>

**D – Operations**

<p>D.1: Compliance principle – A firm should comply with professional standards and applicable legal and regulatory requirements.</p>	<p>These provisions are covered in Part Two: Quality control – Independence section.</p>
<p>D.1.1: The firm should establish policies and procedures for complying with applicable legal and regulatory requirements and international and national standards on auditing, quality control and ethics, including auditor independence.</p>	
<p>D.1.2: The firm should establish policies and procedures for individuals signing group audit reports to comply with applicable standards on auditing dealing with group audits, including reliance on other auditors whether from the same network or otherwise.</p>	
<p>D.1.3: The firm should state in its transparency report how it applies policies and procedures for managing potential and actual conflicts of interest.</p>	
<p>D.1.4: The firm should take action to address areas of concern identified by audit regulators in relation to the Firm's audit work.</p>	
<p>D.2: Risk management principle – A firm should maintain a sound system of internal control and risk management over the operations of the firm as a whole to safeguard the owners' investment and the firm's assets.</p>	<p>These provisions are covered in Appendix One: Governance and accountability.</p>

D.2.1: The firm should, at least annually, conduct a review of the effectiveness of the firm's system of internal control. The review should cover all material controls, including financial, operational and compliance controls and risk management systems.

D.2.2: The firm should state in its transparency report that it has performed a review of the effectiveness of the system of internal control, summarise the process it has applied and confirm that necessary actions have been or are being taken to remedy any significant failings or weaknesses identified from that review. It should also disclose the process it has applied to deal with material internal control aspects of any significant problems disclosed in its financial statements or management commentary.

D.2.3: In maintaining a sound system of internal control and risk management and in reviewing its effectiveness, the firm should use a recognised framework such as the Turnbull Guidance and disclose in its transparency report the framework it has used.

D.3: People management principle – A firm should apply policies and procedures for managing people across the whole firm that support its commitment to the professionalism, openness and risk management principles of this Audit Firm Governance Code.

D.3.1: The firm should disclose on its website how it supports its commitment to the professionalism, openness and risk management principles of this Audit Firm Governance Code through recruitment, development activities, objective setting, performance evaluation, remuneration, progression, and other forms of recognition, representation and involvement.

D.3.2: Independent non-executives should be involved in reviewing people management policies and procedures.

D.4: Whistle-blowing principle – A firm should establish and apply confidential whistle-blowing policies and procedures across the firm which enable people to report, without fear, concerns about the firm's commitment to quality work and professional judgement and values in a way that properly takes the public interest into consideration.

D.4.1: The firm should report to independent non-executives on issues raised under its whistle-blowing policies and procedures and disclose those policies and procedures on its website.

The NAO operates a three line of defence model as set out in the section review of effectiveness in the NAO Annual Report and Accounts 2017-18.

These provisions are covered in Part 2, Quality Control – Our People section, as well as the NAO Annual Report published on our website.

These provisions are covered in our Code of Conduct.

The report on any issues raised under our whistle-blowing policies is a permanent agenda item for the Audit Committee meetings. The whistle blowing policy is published on our website.

## E – Reporting

E.1: Internal reporting principle – The management team of a firm should ensure that members of its governance structures, including owners and independent non-executives, are supplied with information in a timely manner and in a form and of a quality appropriate to enable them to discharge their duties.

Our members of the governance structures were supplied with information in a timely manner and in a form and of a quality appropriate to enable them to discharge their duties.

E.2: Financial statements principle – A firm should publish audited financial statements prepared in accordance with a recognised financial reporting framework such as International Financial Reporting Standards or UK GAAP.

These provisions are covered by our Annual Report and Accounts.

E.2.1: The firm should explain who is responsible for preparing the financial statements and the firm's auditors should make a statement about their reporting responsibilities.

E.2.2: The firm should report that it is a going concern, with supporting assumptions or qualifications as necessary.

E.3: Management commentary principle – The management of a firm should publish on an annual basis a balanced and understandable commentary on the firm’s financial performance, position and prospects.

These provisions are covered by our Annual Report and Accounts.

E.3.1: The firm should include in its management commentary its principal risks and uncertainties, identifying those related to litigation, and report how they are managed in a manner consistent with the requirements of the applicable financial reporting framework.

E.4: Governance reporting principle – A firm should publicly report how it has applied in practice each of the principles of the Audit Firm Governance Code excluding F.2 on shareholder dialogue and F.3 on informed voting and make a statement on its compliance with the Code’s provisions or give a considered explanation for any non-compliance.

This Transparency Report provides the disclosures required by this section of the Code and is available on our website.

E.4.1: The firm should publish on its website an annual transparency report containing the disclosures required by Code Provisions A.1.2, A.1.3, C.2.1, D.1.3, D.2.2 and D.2.3.

E.5: Reporting quality principle – A firm should establish formal and transparent arrangements for monitoring the quality of external reporting and for maintaining an appropriate relationship with the Firm’s auditors.

These provisions are covered by our Annual Report and Accounts.

E.5.1: The firm should establish an Audit Committee and disclose on its website information on the Committee’s membership and terms of reference which should deal clearly with its authority and duties, including its duties in relation to the appointment and independence of the firm’s auditors. On an annual basis, the firm should publish a description of the work of the Committee in discharging its duties.

The Audit Committee terms of reference are published on our website, including membership. The Committee publishes a short description of how it has discharged its duties in the Annual Report and Accounts.

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## F – Dialogue

F.1: Firm dialogue principle – A firm should have dialogue with listed company shareholders, as well as listed companies and their audit committees, about matters covered by this Audit Firm Governance Code to enhance mutual communication and understanding and ensure that it keeps in touch with shareholder opinion, issues and concerns.

The NAO conducts regular meetings with senior management and we undertake internal and external dialogue.

F.1.1: The firm should disclose on its website its policies and procedures, including contact details, for dialogue about matters covered by this Audit Firm Governance Code with listed company shareholders and listed companies. These disclosures should cover the nature and extent of the involvement of independent non-executives in such dialogue.

The NAO does not need to publicly commit to this Code.

F.2: Shareholder dialogue principle – Shareholders should have dialogue with audit firms to enhance mutual communication and understanding.

Not applicable to the NAO because of the NAO’s unique statutory position.

F.3: Informed voting principle – Shareholders should have dialogue with listed companies on the process of recommending the appointment and re-appointment of auditors and should make considered use of votes in relation to such recommendations.

Not applicable to the NAO because of the NAO’s unique statutory position.



National Audit Office