



National Audit Office

National Audit Office

NAO Strategy 2019-20 to 2021-22

DECEMBER 2018

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.

Contents

Foreword 4

Summary 5

Part One

Our vision 6

Part Two

Our strategic objectives 14

Part Three

Our resources 28

Appendix One

Finance tables 36

This report can be found on the National Audit Office website at www.nao.org.uk

For further information about the National Audit Office please contact:

National Audit Office
Press Office
157–197 Buckingham Palace Road
Victoria
London
SW1W 9SP

Tel: 020 7798 7400

Enquiries: www.nao.org.uk/contact-us

Website: www.nao.org.uk

Twitter: @NAOorguk

Links to external websites were valid at the time of publication of this report. The National Audit Office is not responsible for the future validity of the links.

Foreword

1 This is a very uncertain and challenging time for the public sector. Decisions on the future relationship with the European Union (EU) and implications from the United Kingdom's (UK's) exit will affect public services for the foreseeable future. Our strategy reflects how we are supporting Parliament in responding to all the challenges facing government and preparing for the likely challenges of the future.

2 Alongside the UK's exit from the EU our audit environment continues to evolve, and our portfolio of work is growing in size and complexity. The impacts of ongoing financial restraint on public bodies mean that government looks to deliver services in new ways and with fewer resources, through greater delegation to local bodies, complex commercial relationships with the private sector, and with digital technology.

3 In this context, the role of the National Audit Office has never been more important. We inform Parliament and hold departments to account over their spending through our independence and our commitment to high-quality work. We are able to look across government to identify systemic issues and share knowledge, and to review the impact on public service users.

4 Our strategy reflects how we are preparing to respond to the uncertainty in the political landscape and how we propose to use our resources. Our aim is to add real value through our support to Parliament and our wider influence as we focus on the issues of greatest priority, and have the capacity and resources to support accountability and drive public service improvement.

Sir Amyas CE Morse KCB
Comptroller and Auditor General

Lord Michael Bichard KCB
Chairman

Summary

1 The public sector is working against a backdrop of uncertainty and constant change. The UK's exit from the European Union (EU), the outcome of which is still largely unknown, is an unprecedented test for government and public bodies. To allow an orderly departure from the EU, there are more demands on public servants' policy-making capacity and their ability to set up new processes and systems. Public servants will continue to have to plan for multiple outcomes as uncertainty continues. Alongside this, departments and local authorities continue to provide necessary public services and various transformation projects during a period of limited resources.

2 The National Audit Office (NAO) is the statutory auditor of a range of public bodies. We audit the financial statements of all central government departments, agencies and other public bodies. We conclude on the effectiveness, efficiency and economy of public spending. By fulfilling this role, we help Parliament to hold government to account for public spending. In so doing, we challenge the public sector and help to improve how it spends public money and runs itself. Considering the pressures government is facing, our oversight has never been more relevant or essential.

3 In this document, we set out our strategy for 2019-20 to 2021-22 against this context of wider change in the public sector. We describe progress against our long-standing objectives – to apply knowledge, increase our influence and be a high-performing organisation – and how we can best serve Parliament and respond to uncertainty in the outside world that affects us and the bodies we audit.

4 Given the importance of the UK's exit from the EU and the way it will affect all government departments, our four main priority areas for the coming strategy period are to serve Parliament by:

- delivering high-quality work, using modern audit techniques, to address the most challenging issues for the public sector, and in particular exiting the EU;
- providing those we audit with better insight into how they manage and use public money, and responding to feedback for better communication about the benefits of our audit work;
- supporting our people to develop the right skills so in turn they can produce audit work that responds to changes in the public sector, technology and auditing practice; and
- putting in place suitable digital technologies and security to support our people and allow information-led decision-making and effective work practices.

Part One

Our vision

1.1 We help Parliament to hold government to account for spending public money and, in so doing, drive improvements in public services. Our audits of the accounts as well as our wider assurance work provides us with a top-level view of the whole enterprise of the bodies we audit. This allows us to comment on their capability and capacity to deliver their remit and objectives; the effectiveness of their governance of their enterprise-wide controls; and whether they have used the funds voted for by Parliament as Parliament intended. It enables us to provide system-wide, integrated and independent public audit.

1.2 Our audit is 'system wide' because our areas of activity cover the breadth of the public sector, from hospitals to the Ministry of Defence. We are also familiar with all aspects of departments' activities from governance to accountability.

1.3 Our audit is 'integrated' because our work includes not only checking that public bodies' accounts are true and fair, but also whether public spending provides value for money for the taxpayer and is spent in accordance with Parliament's intentions. As a result of both these complementary areas of work, we provide Parliament with a comprehensive understanding of the challenges facing public bodies.

1.4 Our work is 'independent public audit' because the Comptroller and Auditor General and the National Audit Office (NAO) are independent of government. We have the right to choose which areas of public spending to examine and have the right to examine in as much detail as needed those areas we have chosen.

1.5 Therefore, we provide Parliament with a comprehensive view of the public sector because our audit work can be as extensive as needed and reach the parts of the public sector that no others can. Our audit work is neither influenced, confined nor restricted by political edicts of the day, nor by money-making considerations. We conduct our audit work with the interest of taxpayers at heart.

Our three strategic objectives

1.6 Achieving system-wide, integrated public audit relies on achieving our three strategic objectives (**Figure 1**).

- **Developing and applying knowledge:** we carefully plan our work to meet the needs of Parliament, and from this we draw out the insights that are most likely to drive positive change across the public sector.
- **Increasing our influence:** we aim to improve the awareness and the reputation of the NAO held by our audiences, including members of Parliament and the bodies we audit. This way we ensure that our financial audit and value-for-money work leads to public service improvement.
- **Delivering high performance:** we use our funds cost-effectively and aim to get the best from our people.

Figure 1

Our strategic objectives

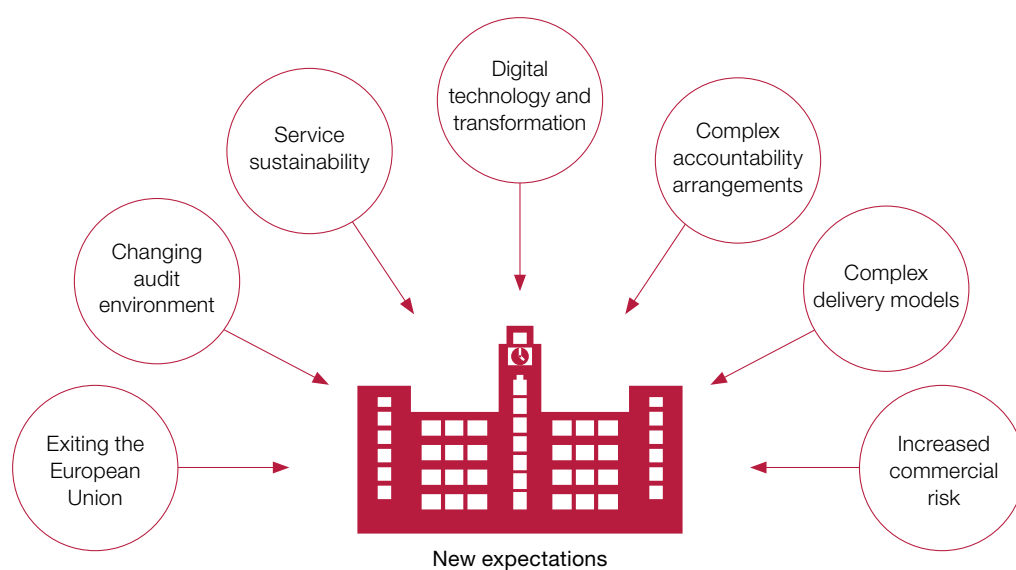


Our challenging external environment

1.7 While our core strategic objectives endure, to serve Parliament fully we must adapt to developments and challenges in our external environment (**Figure 2**). In particular, in the uncertain environment in the coming years, the need for effective and transparent accountability for public spending has never been greater.

Figure 2

Our external environment



Exiting the European Union (EU)

1.8 Exiting the EU presents the civil service with a unique set of challenges.

There are high levels of uncertainty because the final outcome of the negotiations is still unknown, so departments need realistic plans for both an agreed transition period and a scenario where no agreement is reached. Departments are still prioritising their activities and have to work both together, and with stakeholder groups, to tight timescales.

1.9 While some departments will be affected more than others, the result of the decision will be pervasive. There will be new funding streams to replace EU programmes, new regulatory and accountability arrangements to be put in place, legacy IT systems and processes to upgrade, and a body of new UK legislation that will replace EU law. These changes cut across departmental boundaries and such widespread change has little to no historical precedent.

1.10 The operation of the EU single market has meant common legal and regulatory frameworks across many aspects of trade and exchange. Many of these are currently regulated by EU bodies, such as the European Food Safety Authority, the European Medicines Agency and the European Chemicals Agency. Leaving the EU has implications for how the UK will regulate these aspects in future, because the government's stated policy is that the UK will leave the single market and customs union. We anticipate that a number of new UK public bodies will need to be set up to develop and run as substitutes for regulatory arrangements to those carried out by EU institutions.

1.11 One area of considerable public and Parliamentary interest is the UK's financial settlement with the EU. HM Treasury's reasonable central estimate of this is between £35 billion and £39 billion. This is a complex financial transaction and HM Treasury will continue to revise its estimate of payments and liabilities beyond 31 March 2019 as new information becomes available. Some settlement payments, such as contributions to the EU pension scheme, may continue for many years into the future.

Our audit environment

1.12 Our audit environment continues to evolve and, responding to parliamentary requests, our portfolio of work is growing in size and complexity. We work with a wide variety of different delivery models within the public sector and a greater number of more complex commercial bodies than ever before. For this, our people need deeper and wider audit expertise, and we are drawing in specialists to our practice.

1.13 The scope and scale of our financial audit work, as for other auditors, are defined by international standards of auditing, set and regulated by the UK Financial Reporting Council (FRC). Within this regulatory environment, expectations for audit quality are increasing as the FRC promotes continuous improvement in the UK. Over this strategy period, new accounting standards will come into force that will include changing the way leased assets are accounted for and the basis on which revenue is recognised. These will affect how public bodies prepare their accounts and may require them to change their processes for producing their financial information.

1.14 We are therefore called upon to do more financial audit work. At the same time, the technical requirements for our work are increasing because more public bodies are relying on significant estimates within their financial reporting with inherent uncertainties. Our financial audit judgements also often require greater expertise to assess the reasonableness of assumptions made by reporting bodies, which in turn affects the skills, expertise and tools needed by our auditors.

Service sustainability

1.15 During the production of this strategy, government has been preparing a comprehensive spending review. While we cannot be certain of all the implications because the parameters have not yet been announced in full, we know that departments and some services have faced cuts in their funding in the past few years and are still adjusting their spending accordingly. Government has already announced spending increases of up to £20 billion per year for the NHS. It remains to be seen how much additional funding will be made available to the rest of the public services.

1.16 Our reports have shown that some departments and public services have managed to respond effectively to budget reductions while others have struggled to maintain levels of service provision. Budget reductions have had an impact on public service delivery and have contributed to some rising demands on public services or users themselves. For example, the decrease in funding for local services and particularly social care directly affects demand for health services.

1.17 We are also becoming concerned about the signs of pressure on local public bodies. Through our interactions with the local audit profession, we have seen failures in a number of organisations and the number of qualifications has increased each year since 2015-16. The financial sustainability of local public bodies carries implications for the provision of local public services.

1.18 In addition, local services and the health sector continue to be affected by demographic changes, not only an aging population but also some increases in deprivation and complex health issues. Dealing with these will put pressure on many services, including health, local services, schools and police forces.

Digital technology and transformation

1.19 Technology is changing the way that people interact with public services. Successive governments have looked to online services and IT in order to improve the efficiency and effectiveness of government. And the UK has invested heavily in building capacity and capability within the civil service to develop and use technology in designing public services.

1.20 Despite progress in expanding and improving websites and some further automation of processes, the track record of digital transformation has been mixed. Technology continues to improve and many more services are now online, but progress has been incremental and few services have achieved the outcomes expected. While some departments are still running large transformation programmes, others are limiting their transformation programmes as they run short of funding or realise that the savings promised are unachievable.

1.21 Further pressures on government for immediate readiness after EU Exit, combined with concerns about cyber security and the impact of transformation on users, mean that digital transformation risks losing clear direction and commitment within government. Responsibilities for data quality and security lack clear oversight. Combined with a cycle of under-delivery driving further pressures on funding, this means that more ambitious and fundamental changes are dropped in order to meet short-term tactical targets.

1.22 The combination of significant investment in technology and emerging new priorities requiring immediate tactical solutions means that government is building a substantial base of 'technical debt'. Technical debt is essentially when the technical solutions put in place by departments come with an increased risk of these solutions not being able to deliver the enhanced capability needed. As system limitations appear, government continues to adapt services to new policy directions. Moreover, the trade-offs, limitations and rapid production of technical solutions may exacerbate pressures on users who struggle to use services or whose circumstances are poorly managed within existing systems.

Accountability

1.23 Over recent years, government's accountability landscape has become complicated and under considerable pressure. The system of disbursement has many different bodies and structures. There are multiple flows of expenditure and accountability, in particular in the case of complicated delivery structures or commercial arrangements. As a result, it can be difficult to determine who is ultimately responsible for decisions and providing redress when things go wrong. Sustained pressures on departmental budgets can mean that resources are stretched and affect the capability of finance teams who support accounting officers.

1.24 We have seen some improvements in central accountability arrangements across government. For example, HM Treasury has strengthened arrangements in response to our work, including through new mandatory Accounting Officer System Statements (AOSS) for all main departments. Also, based on our published work, the Cabinet Office has set out new standards for the monitoring of grants by departments.

1.25 However, there remain areas where departments need to make improvements. Our work has shown how a wide range of public bodies that spend public money at arm's length from government have lacked adequate oversight by departments. We have highlighted the repeated problem of major projects and programmes being approved by accounting officers when there were clear risks to value for money.

Project and programme management

1.26 The Government Major Projects Portfolio (GMPP) – which includes the most expensive, riskiest and high-profile projects – contains 138 projects with a value of over £500 billion. There are, however, many more projects and programmes across government that are coordinated by individual bodies.

1.27 As we have pointed out in our reports, delivery of projects by government has historically been weak, with recurring issues of cost overruns, time slippage and failure to deliver the intended benefits. There have been repeated instances of poor management, such as an absence of effective mechanisms for prioritising projects across government and for assessing whether departments are able to deliver them. There are issues around poor early planning, lack of consistency in the data used to measure performance, and a lack of accountability for leadership of projects because of the turnover of senior officials. While civil servants' programme management skills are improving, departments are being asked to deliver bigger and more complex projects, so these challenges remain.

1.28 In addition, there are numerous new challenges. Preparations for EU Exit have increased both the need to prioritise and improve portfolio management and the demand for programme and project management professionals. The focus on using infrastructure projects to drive growth and increase productivity has led to higher expectations and greater risks.

Commercial and contracting

1.29 Many complex public services are delivered by private providers through contracts. These commercial relationships account for around 33% of public spending. The government has a mixed record of success in managing these. The reality of providing complex services means that services cannot always be fully captured in a specification or service level agreement. Contracts alone often cannot be relied upon to deliver the savings and improvements required. These difficulties are compounded by the fact that government is not always the end user of the service and thus may not be present at the point of delivery, making it difficult to assess quality of provision. As a result, government has found that it needs to take a much more active role in managing these contracts but, despite some progress, it continues to be hampered by a lack of capacity and skills.

1.30 Government departments have found it difficult to manage contracts effectively, leading in some cases to large losses and failures. Carillion was a strategic supplier to government with around 420 contracts with the UK public sector. After its collapse, the Cabinet Office will ultimately pay the loss on the liquidation, currently estimated at £148 million. The government has also struggled to manage transitions between different providers.

1.31 The complexity of some services also means that often there are only a few credible providers in certain markets. The government aims to reform its buying practices and make procurements easier to access, in order to widen the supplier base. It has also tried to reform the ICT markets to move away from long term contracting with prime providers, towards disaggregated, smaller contracts. More progress is needed to achieve this aim.

Part Two

Our strategic objectives

Developing and applying our knowledge

2.1 In the National Audit Office (NAO) we are in a unique position to comment on the effectiveness of accountability to Parliament. Our work supports parliamentary engagement with government accounts and performance information, and the effectiveness of Parliament's challenge to government's spending plans. This has a direct impact on accounting officers' ability to provide assurance on value for money in complex delivery systems.

2.2 We carefully plan our work to meet the needs of Parliament, and from this draw out the insights that are most likely to encourage positive change across the public sector. Our work is a mix of different types including financial audit and assurance, value-for-money reports, investigations, support to Parliament's committees and advice to international institutions.

2.3 Our priority area of focus is to deliver high-quality audit work that addresses the most challenging public sector issues by adapting to developments in the audit sector and changes in the outside world, in particular the United Kingdom (UK) exiting the European Union (EU).

High-quality work

Financial audit

2.4 We are committed to serving Parliament by providing high-quality financial audits that comply with the standards expected of the top tier of the audit profession. The Comptroller and Auditor General (C&AG), with the support of the NAO, provides an independent audit opinion on some 370 individual accounts across the public sector, including government departments. Through this financial audit work, we are also committed to identifying areas where management can improve controls and processes.

2.5 We will carry on outsourcing part of our audit portfolio to benchmark our performance against other audit firms and align ourselves to developments in audit methodology. Some 20% by value of our audit portfolio is outsourced, which is a fitting balance for the cross-sharing of skills and methods.

2.6 As the external environment is changing, and the bodies we audit are becoming more varied and commercially complex, the capability of our audit practice needs to respond. Within our regulatory environment in the UK, expectations on audit quality are increasing through the Financial Reporting Council (FRC) approach of continuous improvement on audit quality. We are also finding that finance teams in government can lack capacity as departments' resources are stretched. While we have seen some improvements, many departments still provide their accounts late, leading to pressures in delivering our audits.

2.7 The changes that leaving the EU will bring about will have an impact on our financial audit portfolio. Departments will be affected by the closure of specific programmes and many EU functions will need to be carried out by UK public bodies. These changes will need close audit scrutiny and tailored audit programmes to make sure that the costs are estimated and reported accurately. There may be asset impairments or abortive costs associated with programmes closing early, or nugatory activities.

2.8 In addition, new public bodies will be established to administer regulatory arrangements that were previously carried out by EU institutions. We are planning our audit work on the assumption that we will be asked to audit these once the arrangements have been finalised.

2.9 We will also carry on investing in our in-house IT audit capability to make greater use of technology in our audits. This will improve:

- the quality of our work by using automated tools that help our auditors focus their efforts on the important risks to their audits;
- our understanding of business processes and supporting technology; and
- our technology, helping us to keep pace with other audit institutions and government departments.

2.10 In addition, given the increasing complexity and greater prevalence of IT audit and data analytics in government and the private sector, we need to upskill and invest more in professional and technical training. Our approach is to develop our skills base through in-house training to ensure that our people have the skills and knowledge to meet our quality requirements.

Local audit

2.11 We set the Code of Audit Practice. This code sets audit standards for some 950 local authorities and local NHS bodies, and around 10,000 smaller bodies such as town and parish councils. In setting the code and through our interactions with the audit profession, we set out what auditors need to consider when planning their work. In the coming strategy period, we will continue our work to develop and consult on a new code that will need to be issued no later than April 2020.

2.12 Through our interactions with the local audit profession, we are becoming concerned about the signs of pressure on local public bodies. We have seen the high-profile financial failure of a county council with significant implications for local public services. We are also seeing more local public bodies receiving qualified conclusions on value-for-money arrangements from their auditors – as at mid-October, the number of qualifications had increased each year since 2015-16 (local government from 7.1% to 8.3% and local NHS bodies from 29% to 37%). We will report on this in due course in a national study on local auditor reporting.

Value-for-money and other non-financial audit work

2.13 Our legislative powers allow us to produce value-for-money reports that the Committee of Public Accounts uses as a basis for its evidence sessions with accounting officers. We examine the value for money – efficiency, effectiveness and economy – with which public bodies use their resources. We also provide public interest investigations, reports to management, published guidance, and toolkits for audit committees and boards. We respond to correspondence from both members of Parliament and the public.

2.14 Over the past three years, the way we have conducted our non-financial audit work has driven up quality and helped us become more efficient. We are determined to continue to improve the quality and efficiency of our value-for-money and non-financial audit work. We achieve this by:

- exploiting our existing knowledge through re-usable analytics and access to the right expertise;
- streamlining and innovating in our study methods and approaches;
- implementing the Business Improvement Programme, which provided us with the capability to manage our non-financial audit programme more effectively; and
- developing a more diverse product offer, including memorandums and factual shorter pieces.

2.15 Public interest investigations are also now embedded as a core non-financial audit activity. In 2017-18, we published 21 such outputs including three management letters to departments. We conduct investigations to establish the underlying facts in circumstances where concerns have been raised with us, or in response to intelligence that we have gathered through our wider audit and assurance work. Investigations report facts, presenting information in a way that enables the reader to form their own judgements on the stewardship of public funds. Investigations have successfully informed evidence sessions of the Committee of Public Accounts as well as other committees.

Our programme of work

2.16 Our programme of audit work is designed to scrutinise public spending and ensure that taxpayers receive good value for money. Our programme includes work where we compare different areas of the public sector with one another to identify systemic issues of wider importance to the public sector. It also includes work where we aim to share a better understanding of the best way to manage and use public money.

2.17 Over the past year, we have reported on many issues of public interest. We reported, for example, on the Universal Credit rollout and concluded that the larger claims for Universal Credit, such as higher employment, are unlikely to be demonstrable at any point in the future.¹ We also reported on departments' preparedness for EU Exit, concluding that the size of the task facing the civil service meant that some "points of failure" were inevitable.² As we continue into this strategy year, we plan to focus in particular on the following themes.

Exiting the EU

2.18 Whether the UK leaves the EU with or without a deal, there are likely to be significant remaining areas of uncertainty for some time. Dealing with all the implications of EU Exit will be an enormous practical challenge for government departments. We have set up a central team to coordinate the NAO's response to exiting the EU and we will make sure that our resources are focused where they add the most value to Parliament. One of the team's core strands of work has been to examine the models and negotiations around the financial settlement. This team will monitor progress on the settlement beyond 31 March 2019 because of the uncertainties and complexities surrounding this transaction and the parliamentary and public interest in it. We will consider carefully whether to undertake further assurance work on the actual payments once the final settlement is agreed.

2.19 The NAO will need to continue to be responsive to subsequent events and the needs of Parliament. Developments over the next few months are likely to dictate the direction of our work. We have already published a significant body of work to inform both Parliament and the public about the practical implications of the UK's exit from the EU, responding to the clear demand from Parliament, public bodies and businesses for objective, independent information. Initially, we produced shorter, factual briefings as a means of setting out the facts and the landscape for the departments that will be most affected by the exit. Over the past year, we have started to produce more evaluative reports, such as the one on the Department for Transport's progress in preparing for implementing the UK's exit.³ We are planning to continue with this evaluative work but will also produce more reports that show the interdependencies of implementing the UK's exit from the EU across the wider system, such as in our recent report on the Department for Environment, Food & Rural Affairs.⁴

1 Comptroller and Auditor General, *Rolling out Universal Credit*, Session 2017–2019, HC 1123, National Audit Office, June 2018.

2 Exiting the European Union Committee, *Oral evidence: The progress of the UK's negotiations on EU withdrawal*, HC 372, October 2018.

3 Comptroller and Auditor General, *Implementing the UK's exit from the European Union: Department for Transport*, Session 2017–2019, HC 1125, July 2018.

4 Comptroller and Auditor General, *Department for Environment, Food & Rural Affairs: Progress in Implementing EU Exit*, Session 2017–2019, HC 1498, National Audit Office, September 2018.

2.20 At the time of writing this strategy, we anticipate that future focus will be on how the centre of government and individual departments prepare for EU Exit and implement any policy directions. Our reports are likely to shift focus from planning for EU Exit to looking at implementation and operation of services and processes dependent on the outcome of the negotiations. This work is time sensitive and designed around the EU Exit timetable. We will continue to prioritise our work on the departments that will be most affected at a practical level by the exit.

2.21 Government has stated its intention to replace EU structural funding with a UK Shared Prosperity Fund. This is also fundamental to the delivery of the government's Industrial Strategy, and its ambitions for improved productivity and enhanced economic growth. We will want to consider the appropriate timing for reviewing the implementation and effectiveness of the Shared Prosperity Fund once it has been established.

Digital technology and transformation

2.22 Our work on government transformation programmes has consistently highlighted the limitations of technical solutions, and the importance of understanding how processes and behaviours need to change to achieve programme objectives. For example, our report on sustainability and transformation in the NHS concluded that the NHS has received extra funding but this has not provided the stable platform intended from which to transform services.⁵ Increasingly, we have also highlighted the crucial role of data in transformation, and the challenge for government in managing, controlling and using information effectively and securely. We expect our future work to explore the systemic issues with managing data across government as well as highlighting specific challenges in programmes and departments. We will consider data sharing across government and point out where the centre could do more to help address the barriers to this.

2.23 We have also seen evidence that government is building 'technical debt' especially in relation to the preparation of UK's exit from the EU. The technical solutions that are put in place by departments mean that there is an increased risk that these solutions may not be able to deliver the enhanced capability needed. In our report on the Department for Environment, Food & Rural Affairs' progress in implementing EU Exit,⁶ we concluded that the department is running a risk that the basic design and build of its IT system may need significant rework. This is likely to feature significantly in our future audit programme.

2.24 Digital technology affects our ways of working too. While exploring new opportunities and technical developments, we will expand our existing digital audit programmes. To advance our testing of financial systems and our understanding of audited bodies, we have been trialling new analytical techniques in our audits. Our work has identified opportunities to analyse transactions more completely, supporting additional insight and value-adding activities.

⁵ Comptroller and Auditor General, *Sustainability and transformation in the NHS*, Session 2017–2019, HC 719, National Audit Office, January 2018.

⁶ See footnote 4.

Spending restraints

2.25 We foresee the pressure on local services increasing and we will continue to examine sustainability issues. We have built up a portrait of financial stress and falling service performance for many central and local bodies. We have published work, for example, on the financial sustainability of local authorities⁷ and, more recently, on the financial sustainability of police forces.⁸ We see that joined-up decision-making and funding arrangements between connected systems – local government and the health system, for instance – are often absent, leading to ‘cost shunting’ between parts of the systems. In our report, *Discharging older patients from hospital*, we found that there are currently far too many older people in hospitals who do not need to be there.⁹ Without radical action, this problem will worsen and add further financial strain to the NHS and local government. We will continue to consider these issues in our forthcoming work.

2.26 As well as continuing to examine sector-wide sustainability issues, we will consider more specific areas of spending and affordability, such as specific spending streams within the NHS. We will consider the effect that the decision to exit the EU will have on local services.

Accountability

2.27 The issue of accountability will emerge throughout our work programme. We will consider whether individual projects and programmes have clear objectives and governance and accountability arrangements in place.

2.28 Our forthcoming work in the areas of accountability will focus on the accountability landscape for public spending. In particular, we will consider the role of the centre of government’s spending teams and, specifically, the dynamic between them and departments, including their day-to-day interactions and readiness for the next spending review. This work follows our report on the *Spending Review 2015*.¹⁰ We will build on our previous work on single departmental plans to look for evidence of prioritisation, and consider how well they are contributing to business planning and improved decision-making.

2.29 In our work, we have consistently reported on the weak accountability and oversight we have seen in the delivery of local services, in bodies such as local authorities, local enterprise partnerships, combined authorities, clinical commissioning groups and hospital trusts, and the systems within which they sit. We will continue to scrutinise the way that key elements of the local accountability system function in practice, and the nature of the arrangements that central departments have put in place to assure themselves on the operation of the system.

⁷ Comptroller and Auditor General, *Financial sustainability of local authorities 2018*, Session 2017–2019, HC 834, National Audit Office, March 2018.

⁸ Comptroller and Auditor General, *Financial sustainability of police forces in England and Wales 2018*, Session 2017–2019, HC 1501, National Audit Office, September 2018.

⁹ Comptroller and Auditor General, *Discharging older patients from hospital*, Session 2016–17, HC 18, National Audit Office, May 2016.

¹⁰ Comptroller and Auditor General, *Spending Review 2015*, Session 2016–17, HC 571, National Audit Office, July 2016.

2.30 We have previously reported on the government's devolution agenda for local enterprise partnerships and for combined authorities with and without mayors. The government has stated its intentions to devolve further services and infrastructure funding to such bodies. We will continue to monitor how such devolution evolves, and further work may be warranted as it expands in both scale and scope.

Project and programme management

2.31 As we have reported in a range of reports, for example in our report on *Implementing the UK's exit from the European Union*,¹¹ the decision to leave the EU puts pressure on the government's ability to deliver major projects and so increases the importance of prioritising resources. Our work will continue to examine whether departments' decisions to initiate and manage projects throughout their life are based on a clear understanding of the costs and benefits sought, departmental priorities and the effect on their overall portfolio. This is to ensure that transparency and accountability are maintained where we have previously conducted an examination at a particular point in a programme's life and now need to return to that project.

Commercial and contracting

2.32 In the recent years, government departments have made a real investment in their commercial capability and we have ensured that we have matched this with our own capability in auditing contracts and commercial relationships. At the same time, public appetite for transparency and accountability or commercial arrangements continues to be high. Through our work we will consider how government:

- defines its commissioning;
- holds contractors to account for their behaviour;
- understands the expected cost base for the services it is buying; and
- tackles overdependence on a small number of suppliers in key markets.

2.33 Our approach to examining these issues has been to consider this theme alongside effective management of projects and programmes. In the past year, we published work across many departments including health, justice and defence. We have picked up this theme through our public interest investigations, for example in our Investigation into changes to Community Rehabilitation Company contracts.¹² We will continue to use this approach and supplement it with focused examinations of specific commercial relationships where appropriate.

¹¹ Comptroller and Auditor General, *Implementing the UK's exit from the European Union: The Department for Environment, Food & Rural Affairs*, Session 2017–2019, HC 647, National Audit Office, December 2017.

¹² Comptroller and Auditor General, *Investigation into changes to Community Rehabilitation Company contracts*, Session 2017–2019, HC 676, National Audit Office, December 2017.

Support for Parliament

2.34 Our parliamentary relations strategy is to make sure that we serve Parliament – our primary client – by providing high-quality assurance over how public money is spent. We aim to provide the best support we can to Parliament and be well placed to meet its changing needs. Our target is to be recognised by parliamentarians as the ‘go to’ source of expertise and advice to help them scrutinise and hold government to account.

Committee of Public Accounts

2.35 Our relationship with the chair and members of the Committee of Public Accounts (the Committee) is crucial to the success of our strategy. Our reports help the Committee to hold government to account for public spending. In 2017-18, we supported 51 of the Committee’s evidence sessions with written and oral briefings. Since September 2017, we have supported its scrutiny of the government’s progress in overseeing and implementing the UK’s exit from the EU.

2.36 In the first year of the current Parliament, 14 of the Committee’s sessions covered issues relating to the UK’s exit from the EU. Our work supported the Committee in:

- examining the progress in implementing the UK’s exit made by the Department for Exiting the European Union, the Department for Business, Energy & Industrial Strategy, the Department for Environment, Food & Rural Affairs, and the Department for International Trade;
- scrutinising the estimated costs of the UK’s exit; and
- examining a range of other EU Exit-related issues, ranging from immigration and customs arrangements at the border to the impact of exit on the UK’s research and development capabilities, and to the UK’s access to skills and other resources in the future.

2.37 Over the next three years, we expect to continue to support between 50 and 60 evidence sessions a year. This will include ongoing support for the Committee’s scrutiny of the government’s implementation of the UK’s exit from the EU up to and after March 2019, the date of the UK’s withdrawal. To improve the support we provide to the Committee, we will focus on:

- refining our briefings to meet members’ needs by including local data and comparative data for the devolved administrations where possible, and providing more frequent and tailored oral briefings;
- providing greater support to the Committee in following up on recommendations from the Committee’s reports; and
- responding quickly to support the Committee’s scrutiny of emerging issues by producing investigations that are timely and relevant, and in doing so encouraging members to raise potential subjects for investigation with us.

Select committees

2.38 We also support other select committees as part of our programme of wider support for Parliament. At the beginning of this Parliament, we published 25 short guides on government departments, including new short guides on the Department for Exiting the European Union, the Government Office for Science, the BBC and health arm's-length bodies. Short guides summarise what a department does, how much it spends, recent and planned changes, and what issues members of Parliament should look out for when scrutinising government performance. We also provide committee members with an annual overview of the performance of the relevant departments, and support their scrutiny of departments' annual report and accounts through publication of departmental overviews. In 2018-19, we will publish 21 overviews covering the work of individual departments and their 2017-18 annual report and accounts, and major cross-government themes for the relevant committees. We will continue to publish annual updates for committees through to 2021-22.

2.39 We will work systematically to identify opportunities to contribute to select committee inquiries. We provide a range of formal and informal advice and information to select committees to support their inquiries. In 2017-18, in addition to the 25 short guides, we also published bespoke outputs for select committees. Examples included contributions to the Work and Pensions Committee's inquiry into the future of Jobcentre Plus, and the Environmental Audit Committee's scrutiny of departments' approaches to sustainability issues. We also supported a joint Committee of Public Accounts and Public Administration and Constitutional Affairs Committee (PACAC) inquiry into the collapse of Carillion. The C&AG has provided oral evidence to a number of select committees in the past year, including PACAC on sourcing public services, the Treasury Select Committee on the EU financial settlement and the Environmental Audit Committee on environmental governance in June 2018.

2.40 We currently have nine staff on secondment to select committees and to the Scrutiny Unit. Our staff provide vital expertise to committee members as they undertake inquiries and scrutinise the work of government, something we will continue to do. As with the Committee of Public Accounts, we will also seek to build up awareness of our public interest investigations work.

Members of Parliament

2.41 We want all members of Parliament to understand our role and to feel able to actively seek out our expertise on public spending, financial management and service delivery. We will respond to MPs' correspondence and provide assistance where appropriate, including to MPs' staff. During 2017-18, we provided 108 responses to correspondence from MPs. Roundtable briefings for parliamentarians on issues such as defence spending have been well received. We will work closely with the House of Commons Library and the Scrutiny Unit, including through secondments.

Integrated public audit

2.42 Bringing financial audit and value-for-money work together can provide Parliament with a deeper understanding of the challenges facing individual departments and the wider public sector. In 2017-18, the Committee held evidence sessions on value-for-money studies and investigations that had arisen from areas identified by financial audit, like the *Investigation into the Disclosure and Barring Service*.¹³ In addition, the Committee took evidence on an increasing number of departmental accounts including those of the Department for Education, the Department of Health & Social Care, the Whole of Government Accounts and HM Revenue & Customs. We will work with the Committee of Public Accounts and other committees to increase the awareness of our financial audit work within Parliament and provide assistance to MPs dealing with complex financial matters and interrogating government accounts.

Increasing our influence

2.43 For our work to fulfil its potential, it is important that we always seek to increase our influence. We aim to improve the awareness and opinion of the NAO held by our audiences, including MPs and the bodies we audit. The aim is to effect positive change, so that government is more likely to implement our recommendations and look to us as a source of expertise. Our main area of focus is to respond to feedback from those we audit for a better understanding of the best way to manage and use public money, and for better communication about the benefits of our audit work.

Delivering value in an uncertain external environment

External communications

2.44 Our external communications help us to be recognised as a trusted provider of high-quality audit work. To date, our focus has been on improving the mix and quality of our digital communication channels, such as our website, our social media presence and other digital communications, such as our e-newsletter and blog. We have also worked to achieve higher brand awareness, communicate relevant findings from our audit work in the local government sector, and keep a high-level of quality press coverage for all our audit work. We also take part in external engagements, increasingly on digital topics, and we speak at conferences as well as contributing to publications.

2.45 We are now refreshing our external communications strategy. Communication methods and channels are constantly changing, as are the needs of our audiences. Our new communications strategy will take account of these changes and ensure that we engage our audiences in ways that work for them. This will bolster our positive reputation for our audit work and the NAO's brand.

¹³ Comptroller and Auditor General, *Investigation into the Disclosure and Barring Service*, Session 2017–2019, HC 715, National Audit Office, February 2018.

2.46 Through our annual feedback survey of audited bodies, those we surveyed told us that they continued to particularly value our cross-government perspective and would like us to help public services improve by sharing good practice and guidance. To that end, in the coming strategy period, we will produce a few signature knowledge products on cross-cutting topics. These will be short, accessible publications designed to help public bodies improve their performance.

Managing the value of our work

2.47 Alongside our primary responsibility towards Parliament, we are committed to driving improvement in the public sector. This is significantly assisted by actively managing the continuing discussion with those we audit about how our work can and does deliver value against the issues that matter. Engaging in a dialogue about our audits and their value helps us become better auditors by better understanding those we audit. It also allows us to identify opportunities to help those we audit to deal with their challenges through our expertise and thematic knowledge.

2.48 This is why last year we started a programme of engaging in discussions with our audited bodies about the value of our audits, both individually and overall, through meetings at various departmental levels. In 2017-18, we made good progress in engaging with accounting officers and officials at all levels through more interactions on specific pieces of work, for example emerging findings and post-study meetings.

2.49 This has led to our audited bodies publicly recognising the value of our work. For example, the Bank of England recognised the value of our work in its Annual Report and Accounts, writing “The NAO’s first review of the Bank was a valuable reminder of the importance of keeping costs under scrutiny and of providing clarity upfront about the aims of planned investments”. The BBC board members were very grateful for the way that we approached their audit and for the professionalism and skills of the team, both on the public service and the commercial audits. We have similar examples of this type of systematic engagement with accounting officers and officials beyond the audit cycle and through dissemination of findings and good practice.

2.50 There is, however, more to do to establish this deeper engagement as routine across our organisation. We will therefore engage with all the departments during this strategic period and ensure that we are explaining effectively how our audit work has helped our audited bodies. We will continue to hold two-way conversations with those we audit about how our work – both financial and non-financial audit – is of benefit. We will work on establishing longer-lasting relations at various levels in the departments to discuss with our audited bodies how they can best respond to our recommendations and those of the Committee of Public Accounts. We will identify opportunities where audited bodies could benefit from our cross-government and public audit insight and perspective, beyond our standard audit engagements.

2.51 Our aim is that, by the end of this strategy period, talking about and recognising the value of our work will become ‘business as usual’ for audited bodies and audit teams. We expect to see such discussions lead to better-quality relationships between us and our audited bodies, and ultimately greater benefits for taxpayers as public bodies use our recommendations and insights to make sustainable improvements to their services. In the long term, we would also expect to see improvement in the feedback we receive from our audited bodies.

2.52 We will also continue to assess where our work has resulted in a financially quantifiable net benefit improvement to the public sector. The audited bodies concerned confirm these financial impacts, and our external auditor provides assurance on them. During the calendar year 2017, as detailed in Annual Report and Accounts 2017-18,¹⁴ our financial impact was £741 million, which is a saving for the taxpayer of around £11 for every pound we spend.

Delivering high performance

2.53 We are committed to the efficient use of public funds and making sure that we maximise the value of what we do. Our ability to be a high-performing organisation is not only predicated on efficient use of our resources but also on our people’s distinctive knowledge of and insight into the public sector. Our main areas of focus are:

- supporting our people to develop the right skills, so they can produce audit work that responds to changes in the public sector, technology and auditing practice; and
- putting in place digital technologies that both increase the capability of our business and make sure that the information and data we use in our work are secure.

Supporting our people

2.54 Our people remain our greatest asset. We provide high-quality work to Parliament because we invest in recruiting, developing and keeping the right calibre people. Each year, we recruit some 70 to 80 graduates and school leavers and support them in gaining their professional accounting qualification. We also support all our people with ongoing learning and career development.

2.55 NAO staff are unique in that they are highly trained experts in public financial management and have a broad view across the whole of the public sector. In our experience, it is more efficient to retain our people with their knowledge already built up than to invest in recruiting and retraining new individuals, who may not be of the same calibre, to replace lost staff.

2.56 Investing in our people is critical to our success. We will therefore refresh our office-wide learning and development strategy, setting out how we will use our learning and development offer to attract and keep high-quality staff.

2.57 We want to embed a culture of continuous learning and development, whereby we help our people to keep their skills at the desired level. To achieve this, we need to support them to further develop their skills across the following areas.

- **Technical and methodological skills:** we need to have even better technical and methodological skills, at all levels, to keep pace with expectations of our work.
- **Digital skills:** our work needs to be up to date with digital advancements. Parliament and our audited bodies expect us to keep pace with the new technological tools, techniques and systems, that are already changing the audit industry.
- **Sector and cross-government knowledge:** in order to be recognised as providing valuable audit work our people need to have a good understanding of their audited bodies' operating environments and their work to modernise and digitise their organisations. They also need the skills to bring our cross-government expertise and integrated public audit perspective to bear as those we audit would like us to.
- **Personal effectiveness skills:** employees expect an inclusive working environment and managers who know how to bring out the best in our people. Our people need to continuously improve their management skills to provide such an environment.

2.58 Over the strategy period, we will also implement our refreshed diversity and inclusion strategy. This builds on the progress we made with our previous strategy, which expired in 2018. To date we have improved Black, Asian and Minority Ethnic (BAME) diversity in our graduate intake, co-founded the Access Accountancy initiative to improve social mobility in the accountancy profession, implemented a flexible working culture, and appointed Dignity at Work leads and mental health first-aiders to provide support to our staff.

2.59 However, our new diversity and inclusion strategy recognises that we have made slower progress on other aspects. While all protected characteristics remain important to us, we have prioritised gender, ethnicity and disability in the first instance to help us make greater progress in areas where we know previous interventions have not resulted in sustained improvement.

Digital and cloud-based technology

2.60 Our people need a secure and well-integrated digital environment that enables them to deliver high-quality audits and to add value to Parliament and our clients. We recently completed our Business Improvement Programme that replaced legacy IT assets with a fully integrated cloud-based finance, HR and project system, introducing new streamlined workflows and project management tools. We are now moving other technology office applications to the cloud, including communication and information management systems. Our strategy to make this transition is based on a number of clear principles.

- **Security:** our access to information and data in government is fundamental to our role. With the risk of cyber security breaches increasing, cloud platforms offer a more secure environment than we can maintain in-house. This is particularly important following the decision to close the public sector network in 2019, which provided a secure digital communication channel for the UK public sector.
- **Capability:** by giving ourselves access to much bigger IT platforms, we increase the volume and speed at which we can process and store data. By purchasing this as a service, we benefit from continual updated technologies and good industry practices.
- **Value:** cloud services provide simplicity and agility. We can flex our IT and business processes as we need them, rather than entering into long-term design commitments that need to be hosted and maintained on our premises.

Part Three

Our resources

3.1 Our external environment is both challenging and changing. The process of exiting the European Union (EU) dominates the business of government and will have wide-ranging effects across the public sector for many years into the future. Our audits are becoming more complex. We audit more large bodies, and the introduction of new financial reporting standards is a challenge for finance teams across government that have capacity and capability gaps. There are wider challenges in respect of the impact of digital technology in government, the consequences of ongoing pressure on departmental budgets, and the increased use of commercial partners to deliver public services. All this means we now work in an environment that is uncertain and unpredictable.

3.2 In this environment, the importance of the National Audit Office's (NAO's) work has never been greater. We are an independent, expert source of assurance and provide Parliament with evidence-based, timely analysis with which it holds government to account. We need to have the resources to do our work to the right level of quality, and which allow us to respond to new priorities as they arise. Our request for the next three years are summarised in **Figure 3**, with more details in Appendix One.

3.3 Our requests have been developed in direct response to the demand for our work and:

- include our programme of work dealing with the UK's departure from the EU, including continued review of the financial settlement;
- reflect the increased complexity of our existing financial audit portfolio, which includes more commercial bodies and the challenge of overseeing new reporting standards;
- adjust for increases in the number of audits we are asked to do each year, including an expansion of the BBC group of companies and the Student Loans Company;
- support a wide programme of value for money and investigations that allows us to continue to help Parliament to hold government to account, in particular during the process of exiting from the EU, where there is a risk that other government activities will receive less scrutiny;
- set out our ongoing investment in the use of technology and data analytics in our work, so that we continue to provide Parliament with high-quality products and audits, and keep pace with changing technology in departments; and
- allow us to invest in our people, making sure that we have the right skills and capability to discharge our statutory responsibilities and respond to changing priorities and the evolving nature of our work.

3.4 We are monitoring the development of new accountability and audit arrangements in respect of fiscal devolution. We will have further discussion with the Public Accounts Commission on the impact of this on our work when it becomes clearer.

Figure 3

Forward resource plans

	2018-19 Budget (£m)	2019-20 Proposed (£m)	2020-21 Proposed (£m)	2021-22 Proposed (£m)	Total
Total spend	88.1	89.6	90.7	91.8	
Income	20.6	21.3	21.4	21.4	
Net spend	67.5	68.3	69.3	70.4	
Change year on year (£m)		0.8	1.0	1.1	2.9
Percentage change (%)		1.2	1.4	1.5	4.2
Percentage change inflation adjusted (%)					-0.7

Breakdown of resource by our work

3.5 Our resource plans cover the full portfolio of financial audit, value for money, investigations, and other work we do to support Parliament. **Figure 4** shows how our resources are allocated to our different activities and work streams.

Figure 4

Use of resource by type of work

	2018-19 Budget (£m)	2019-20 Proposed (£m)	2020-21 Proposed (£m)	2021-22 Proposed (£m)
Audit and assurance	52.6	55.6	56.3	56.8
Value for money	18.1	16.5	16.8	17.0
Investigation and insight	10.9	11.0	11.1	11.3
Support for Parliament	5.4	5.4	5.4	5.4
International relations	0.9	0.9	0.9	0.9
Comptroller function	0.2	0.2	0.2	0.2
Total spend	88.1	89.6	90.7	91.8

Exiting the EU

3.6 Our response to the UK's departure from the EU needs careful coordination and affects all our work streams. Our reports have to be planned and timed to ensure that they provide Parliament with the necessary assurances at the right moment. We aim to make an impact but we are also aware that we do not want to undermine the UK's position in discussions with the EU. The selection and planning of work requires very careful supervision and a deep understanding of what is happening across the whole system. We have established a central oversight team, drawn from our audit and value-for-money communities, to help plan and make sure that our response to what is a complex and cross-departmental change programme is effective. This work will be ongoing across our strategy period.

3.7 A central component of this team's work will be to directly carry out the assurance work on the financial settlement, for exiting the EU. We provided Parliament with independent assurance on the methodologies and assumptions underpinning the projected cost of the settlement, and will continue to publish reports and briefings in 2018-19. We intend to continue our work on the financial settlement beyond 31 March 2019, as negotiations and valuations continue throughout the expected transition period. Therefore, our forward budgets include an allocation of £1 million per year for central work.

3.8 The process of leaving the EU will also directly affect our wider financial audit portfolio. In individual accounts, we will need to make sure that related costs are accounted for and disclosed correctly. There will be difficult judgements to be made on how certain types of expenditure will be treated. These will depend on the final departure process. There are likely to be many commitments entered into, which will require immediate recognition as an expense in the accounts.

3.9 The planning assumptions that underpin our resource proposals reflect our best knowledge at the time of writing. This applies particularly to the UK's exit from the EU for which we are planning on the basis of an orderly exit, with a transitional period lasting until 31 December 2020. However, clearly this could change quickly and, if it does, then we will need to respond appropriately. We need to be responsive to the needs of Parliament and we will continue to discuss our resource plans with the Public Accounts Commission as events unfold.

Audit and assurance

3.10 Our plans reflect the changes that we see taking place in our audit portfolio. These include new bodies that we have been asked to take on, such as the Student Loans Company and four BBC production companies. However, our plans do not include any new regulatory bodies that will be established once we have left the EU. At the time of writing, we do not have enough knowledge of what the regulatory environment will look like to plan for this with any confidence, but these could be substantial additional commitments.

3.11 Our plans also reflect the wider trends we see across our audit work. These include increased expectations of our financial audit where the Financial Reporting Council (FRC) promotion of continuous improvement in quality. The scope of our financial audit work is very tightly defined by international standards of auditing and is also wider than other audits in order to provide Parliament with assurance on regularity. We are committed to providing Parliament with a high-quality financial audit, and we undergo a full audit quality review by the FRC each year. We find we need to spend more time on our audits to guarantee quality.

3.12 New financial reporting standards mean that accounts will be more complicated both to prepare and to audit. Recent pressures on departments' budgets have at times left their finance teams under-resourced and facing capability gaps. This manifests in the late delivery of accounts and a lack of readiness for new accounting standards. This will adversely affect the timetable and quality of account preparation. Unexpected delays will make it difficult for us to reschedule work in an already busy period; poor-quality accounts and supporting papers will mean more work for our audit teams. We need to make sure that we have the capacity to respond to these challenges.

Non-financial audit work

3.13 We have made efficiencies in this area of our work, which is where the impact of our recent investment in business improvement is realising benefits. We see increased productivity in our teams because better planning and allocation tools, supplemented by detailed reports and analytics, allow us to deploy people quickly between projects, minimise downtime and focus our non-financial audit work to areas that matter most to Parliament and the bodies we audit. However, we propose to reinvest these efficiencies in our financial audit work.

3.14 We are confident that our productivity gains mean that we can reduce our spend in this area while still producing a full range of value-for-money studies and investigations, responding to correspondence and providing direct support to Parliament. These efficiencies have allowed us to focus our non-financial audit work on the highest priority areas, and increase our influence and impact. We will not cut back on the breadth or quality of the work we do for Parliament. We have very rigorous internal and external quality standards and checks on our non-financial audit work, and these will be maintained.

Our people

3.15 Our people are our key asset and where we most invest. Our salary and staff-related costs account for the majority of our cost base, at around 70%. We currently employ 820 full time equivalent staff, and we consider this to be the number we need to carry out our existing range of statutory responsibilities.

3.16 Historically we have sought savings and efficiencies by looking for reductions in headcount. However, for the next few years, we do not think this is sensible in the context of the pressures and demand for our work. We plan to retain the knowledge and skills we have built up and, in light of the new bodies we have been asked to audit, we propose to increase our staffing levels to 825 over the strategy period (**Figure 6**, Appendix One).

3.17 We need to be sufficiently flexible to respond to a fast-moving external jobs market, with the quality and skills of our people continuing to prove attractive to our competitors. In addition to retaining those who have progressed their careers through our accountancy training, our resource model also relies on our ability to secure quickly the specialist skills we need to deliver our audit work. Having a sufficiently attractive reward package in place will therefore remain a key factor in ensuring that the NAO is appropriately resourced over the period of the strategy.

3.18 Last year we agreed an average pay award of 2% for the year, which was based on our external benchmarking of inflation, earnings growth and latest pay settlements in comparator organisations. Our approach was to apply this as a differentiated pay award, with those paid in the lower half of their pay range receiving higher percentage increases than those at the higher end of the range. This has been successful in reducing our pay gaps and creating a fairer and more equitable approach to pay, which has also helped retained our younger talent. Our staff turnover rates are currently in line with expectations and are allowing us to plan for the challenges ahead. With evidence that our pay policy is achieving its aims and with external market conditions similar to those that applied last year, we have made the same budget assumption of a 2% pay award in future years. We will again use it to target awards on those paid in the lower half of their pay range.

3.19 Our practice in recent years has also been to include flexibility in our budget that would allow us to make pay adjustments in year by another 1% if we needed to do so. However, we have managed our staff numbers without using this and, in line with our commitments, will return it unspent. It is clear that we now face much more uncertain times and the demand for our work could increase rapidly at short notice. If we need to respond quickly to parliamentary requests, we may need to scale up operations quickly and buy in skills and experience at short notice. It is important that we are in a position to do this or have further pay award flexibility, and it is therefore prudent to retain this level of flexibility in our staffing budget.

3.20 Staff costs (Figure 6, Appendix One) include salaries, social security costs and pension contributions. Most of the NAO employees past and present are covered by the provisions of the Civil Service Pension Scheme that is managed by the Cabinet Office. The NAO pays contributions into these schemes at agreed rates. Periodically these rates are revised by the Cabinet Office on the basis of actuarial advice provided by the Government Actuary's Department. We understand that a review has been completed recently but that the results are not yet available. However, early indications suggest that the results will show the contribution rate that employers pay towards the schemes will need to increase. If this is the case, then NAO staff costs will also increase. These increases are not yet included in our forward proposals because we do not yet know what the actual changes to contribution payments will be. We expect to have this information by the time we meet with the Commission in March and will be able to amend our budgets at this stage.

Efficiency

3.21 We are on track to deliver the efficiencies from our recent business improvement programme and the conclusion of our internal corporate service review.

3.22 Our Business Improvement Programme was rolled out in September 2016, with follow-up work carried out through 2017. This marked the successful implementation of fully integrated cloud-based finance, human resources and project systems to replace legacy IT assets. This was the subject of an external value-for-money study published last year, which concluded that the benefits were realised in line with our plans. These benefits manifest in smarter planning, with more efficient allocations of staff between projects, meaning we can manage the variable elements of our portfolio more effectively. This allows us to reduce the resources we need for our value-for-money work without affecting the quality or the breadth of our output (Figure 4).

3.23 We are also on track to reduce the net cost of our corporate overheads by £3 million against our baseline of 2015-16. This is in line with the findings of our internal corporate service review. It has been achieved despite the fact that the size of our portfolio of work has continued to grow over the same period, with new audits such as the BBC and Network Rail.

Investment

3.24 We see technology as a central part of our financial audit methodology. By using it more effectively, we will increase the value that we provide with our audits. In line with other firms in the industry, we will continue to develop this work stream as a priority. We are also aware that our audit requires us to analyse and process data from a wider range of government activity, and we are committed to making sure that our own systems and data stores are secure from external threats.

3.25 We will therefore maintain our annual investment in the use of technology to augment our financial audit approach (**Figure 7**, Appendix One). This is essential to our being able to audit the new technologies that are increasingly used by our client bodies (for example, cloud-based computing) and ensuring that our own use of technology stays in line with developments in the audit profession. In this way, we can make sure that Parliament receives audit services that are comparable in quality and capability to those offered by the top commercial audit firms. We will invest in the following:

- Data analytics software, which extracts, processes and highlights anomalies in large quantities of data. This approach was deployed with great success in the first year of auditing the BBC. The ability to quickly identify problem areas and potential control failures through data analytics means that our audits are of higher quality and provide better insight and value to governing bodies.
- Training to make sure that audit teams have the skills to audit emerging technologies and the increasing digitalisation and automation of process. Examples include the widespread adoption across central government departments of cloud-based accounting systems, coupled with department-specific system changes, such as a new customs declaration system, a new visa system and digital passport system, and the automation of court systems with its knock-on effects on court fees and fines. Our IT audit work supports the assurance we get over the income that government receives from these systems.

3.26 Data and IT security also continue to be carefully managed, and our budget includes annual investment in our information security architecture and plans to strengthen our policies and procedures. There is a small budget reduction next year in these costs as we complete a period of transitioning away from the central government public sector security network.

Income

3.27 We receive income from UK and international fee-paying audits, the provision of services to international and overseas audited bodies, secondments to other organisations, and rental of surplus space at NAO headquarters (**Figure 8**, Appendix One). We anticipate an increase in income over the strategy period from the fees we charge for our work, as we take on more audits and from the additional rental of our office space.

3.28 We have had success with our reorganisation of space in our London building. We were able to make two additional floors available for rental from 1 April 2018 in line with our earlier proposals. While we are dependent on market factors outside our direct control, we aim to have all our surplus space rented out by 31 March 2019.

Asset management

3.29 Each year we require a capital budget to purchase IT assets and make any enhancements to the London property whose use extends beyond one year (**Figure 9**, Appendix One). These budgets are based on detailed asset plans that show the timetable for replacing physical assets, such as laptops, mobile phones and desk-top equipment, which takes place on multi-year cycles. Capital work on the building, which is a listed historic property, may arise at short notice. These budgets, therefore, reflect all known future capital plans. However, we may need to revisit these if further work on the building is required.

3.30 Because these assets are used for more than one year, the cost is allocated across the period of time over which they are used in the form of a depreciation charge, which is reflected in resource requirements (Figure 7, Appendix One).

Appendix One

Finance tables

Figure 5
Financial summary

	2018-19 Budget (£000)	2019-20 Proposed (£000)	2020-21 Proposed (£000)	2021-22 Proposed (£000)
Staff costs	61,300	63,300	64,400	65,500
Non-staff costs	26,805	26,325	26,305	26,265
Total spend	88,105	89,625	90,705	91,765
Income	20,600	21,300	21,400	21,400
Net spend	67,505	68,325	69,305	70,365

Figure 6
Staff costs and numbers

	2018-19 Budget (£000)	2019-20 Proposed (£000)	2020-21 Proposed (£000)	2021-22 Proposed (£000)
Salaries	43,300	44,900	45,800	46,700
Social security costs	5,000	5,200	5,300	5,400
Pension costs	9,500	9,800	10,000	10,200
Direct staff costs	57,800	59,900	61,100	62,300
Staff-related costs	2,800	2,800	2,700	2,600
Staff benefits	500	390	390	380
Apprenticeship levy	200	210	210	220
Total staff costs	61,300	63,300	64,400	65,500
Total staff numbers	820	825	825	825

Figure 7
Non-staff costs

	2018-19 Budget (£000)	2019-20 Proposed (£000)	2020-21 Proposed (£000)	2021-22 Proposed (£000)
Professional services	11,800	11,800	11,800	11,800
Travel	2,280	2,280	2,380	2,380
Audit technology	600	560	540	500
Office costs				
Facilities management	4,800	4,700	4,700	4,700
Office supplies and equipment	2,470	2,300	2,300	2,300
Recruitment and professional training	1,520	1,470	1,370	1,370
Data security	535	415	415	415
External auditors – audit fee and other work	100	100	100	100
Other administration costs	100	100	100	100
Operating lease rentals	200	200	200	200
VAT recoverable	-800	-800	-800	-800
Tax expense	200	200	200	200
Total office costs	9,125	8,685	8,585	8,585
Depreciation and amortisation				
Depreciation on property, plant and equipment	2,140	2,140	2,140	2,140
Depreciation on other items	660	660	660	660
Amortisation	200	200	200	200
Total depreciation and amortisation	3,000	3,000	3,000	3,000
Total non-staff costs	26,805	26,325	26,305	26,265

Figure 8

Income

	2018-19 Budget (£000)	2019-20 Proposed (£000)	2020-21 Proposed (£000)	2021-22 Proposed (£000)
Audit fees – UK	17,100	17,600	17,600	17,600
Audit fees – international	400	500	500	500
International technical cooperation	300	400	400	400
Secondment income	600	600	600	600
Rental of office space	2,200	2,200	2,300	2,300
Total income	20,600	21,300	21,400	21,400

Figure 9

Capital expenditure

	2018-19 Budget (£000)	2019-20 Proposed (£000)	2020-21 Proposed (£000)	2021-22 Proposed (£000)
IT equipment and licences	800	800	800	800
Property, plant and equipment	600	200	200	200
Total capital expenditure	1,400	1,000	1,000	1,000

© National Audit Office 2018

The material featured in this document is subject to National Audit Office (NAO) copyright. The material may be copied or reproduced for non-commercial purposes only, namely reproduction for research, private study or for limited internal circulation within an organisation for the purpose of review.

Copying for non-commercial purposes is subject to the material being accompanied by a sufficient acknowledgement, reproduced accurately, and not being used in a misleading context. To reproduce NAO copyright material for any other use, you must contact copyright@nao.gsi.gov.uk. Please tell us who you are, the organisation you represent (if any) and how and why you wish to use our material. Please include your full contact details: name, address, telephone number and email.

Please note that the material featured in this document may not be reproduced for commercial gain without the NAO's express and direct permission and that the NAO reserves its right to pursue copyright infringement proceedings against individuals or companies who reproduce material for commercial gain without our permission.

This report has been printed on Evolution Digital Satin and contains material sourced from responsibly managed and sustainable forests certified in accordance with the FSC (Forest Stewardship Council).

The wood pulp is totally recyclable and acid-free. Our printers also have full ISO 14001 environmental accreditation, which ensures that they have effective procedures in place to manage waste and practices that may affect the environment.



National Audit Office