

# Transparency Report

## 2018-19

JUNE 2019



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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) 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 a financial impact of £539 million in 2018.

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National Audit Office

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# National Audit Office **Transparency Report** **2018-19**

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Article 13 of Regulation (EU) No537/2014.

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This report can be found on the  
National Audit Office website at  
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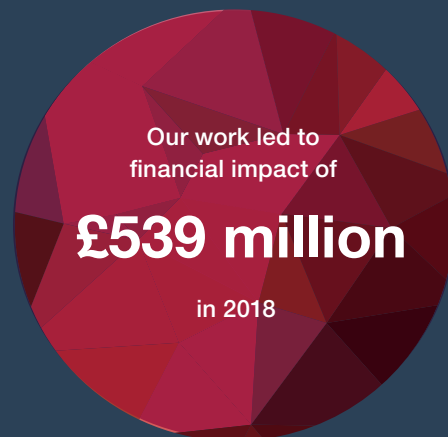
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# 2018-19: Our year in highlights



## We make a difference to people's lives

An important part of our work is to drive positive change in the way public services are delivered to make a real difference to people's lives. For example, the recommendations from our report on *Major Trauma Care* in England have been associated with significant improvements in both the care process and outcomes of patients after severe injury, leading to a significant increase in the odds of survival for trauma patients treated at hospital. In *Rolling out Universal Credit* we found that some claimants had struggled to adjust to Universal Credit and had suffered difficulties and hardship during the rollout. One-fifth of claimants were not paid on time. We recommended that the programme should not expand



before business-as-usual operations can deal with higher claimant volumes – an approach which was taken.

The recommendations from our value-for-money reports and investigations help government improve public services; 94% of the recommendations we have put to departments since 2014 have been accepted.



## Our people are our greatest asset

We care about what our people think and typically we achieve excellent response rates to our people survey (77% in 2018). The results continue to show strong levels of engagement from our people, which compare favourably with the organisations we benchmark against. We have worked hard to improve how we support our people through creating a more flexible work environment, and developing our ways of working.

During the year we have launched a new diversity and inclusion strategy which focuses on gender, race and disability

to enable us to make a sustained and accelerated change over the next three years.

We are a recognised provider of the ACA professional training scheme; 83.4% of our trainees passed the Professional Stage examination at the first attempt (in line with the national average) and 94.3% passed the Advanced Stage examination, also at the first attempt, which is significantly above the national average of 85.2%.



## We are an independent voice

The aim of our EU exit work is to provide an independent and authoritative voice on EU exit for Parliament; to have a positive impact on how departments prepare for and deliver Brexit; and to support Parliament's understanding of the financial settlement and ensure there are appropriate accountability arrangements in place. To achieve this aim we published 11 pieces of work on EU exit including two reports on the UK's financial settlement with the EU.

The Committee of Public Accounts held 61 evidence sessions to tackle issues affecting the delivery of public services, all of which were informed by the evidence we presented.

Our reports have also provided select committees with authoritative and independent evidence to help inform their inquiries, for example the Business, Energy & Industrial Strategy Committee's inquiry into *Rolling out Smart Meters* and the Treasury Committee and the Work & Pensions Committee's joint inquiry into Motability. In addition, we produced bespoke reports for the Environmental Audit Committee on *The packaging recycling obligations* and *Environmental metrics*.



## We audit all of government spending

With the support of the National Audit Office (NAO), the Comptroller and Auditor General (C&AG) certified the accounts of all government departments and commercial entities such as the BBC, financial services companies and other public sector bodies.

390 accounts certified  
covering more than

**£1.7 trillion**

of public income  
and expenditure

**66 major  
outputs**

covering value-for-money  
reports and investigations  
including reports on local  
public services such as  
health and social care

## We also audit a small number of international organisations

The C&AG serves as the external auditor of the World Intellectual Property Organization and the Pan American Health Organization. The C&AG chairs the UN Panel of External Auditors.

# Foreword from the Comptroller and Auditor General



**Sir Amyas Morse**

Comptroller and  
Auditor General  
National Audit Office

Welcome to our 2019 National Audit Office *Transparency Report*, which explains how we carry out our audits and ensure that our work meets the needs of Parliamentarians and taxpayers.

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 whole system of government, while ensuring independence from those we audit.

We aim to shed light on matters of public interest, to help parliament hold government to account and to promote public service improvement. Time and again I have seen how transparency, while not instinctive to government, is critical to improving performance. It is therefore right that we strive to lead by example in the way in which we report on both our successes and where we have further work to do.

My term as C&AG is due to end on 31 May 2019, when I will have completed ten years in the role. Looking back, the environment we find ourselves in has changed dramatically over this time – the fall-out of the financial crisis, austerity, devolution and the prospect of the UK's withdrawal from European Union (EU) have all brought change and volatility to the public sector. We have sought to hold those who run public services to account but also to help them respond positively to the range of challenges that they face through our delivery of high-quality system-wide, integrated public audit, providing sound rationale and robust information analysis.

Our portfolio of work means we audit more than £1.7 trillion of public income and expenditure. In recent years, our core audit work has expanded to include big commercial entities such as the BBC, Network Rail and financial service companies. We are committed to delivering high-quality audit work, and welcome the external challenge provided by those who inspect our audit work. In addition, through independently commissioned surveys, we seek feedback on the quality of our work from our audited bodies and MPs. We value the insights that these surveys give us, and take action as appropriate to further strengthen the quality of our audit work.

The high response rate from the audited bodies to the recommendations we make, as well as the thousands of requests we receive from members of Parliament and the public for information on issues affecting our nation is a strong measure of the impact of our work, and the difference it can make to people's lives. Nonetheless, we are always looking to enhance the impact we have further, to improve the quality of public service.

Looking ahead, public audit will continue to face a rapidly changing environment. Whether this is regulatory changes following the UK's departure from the EU, or the introduction of new financial reporting standards, our audit practice must continue to respond appropriately to emerging risks in public sector finances, and to the audit profession itself. We continue to invest in supporting our people, modernising our audit to take advantage of new technologies, and to respond to digital advances within our client base, to equip us for this challenge.

Our *Annual Report and Accounts* for 2018-19 sets out our performance during the year. This *Transparency Report* complements our *Annual Report and Accounts* by showing how we prioritise and pursue best practice and the highest professional standards in our audit work, and the significant impact it had during the year, both in terms of public sector improvement and transparency in the way public funds are spent, on behalf of Parliament and ultimately taxpayers. This *Transparency Report* demonstrates we are a small organisation with a big impact. It has been a privilege to lead the NAO during my tenure as C&AG.



# Part One

## OVERVIEW

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

### About us

**1.1** The NAO scrutinises public spending for Parliament. Its public audit perspective helps Parliament hold government to account and improve public services. To achieve this, the NAO provides system-wide, integrated and independent public audit, drawing on the distinctive framework of rights set out by Parliament.

**1.2** 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 NAO staff are independent of government.

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

### Comptroller and Auditor General

**1.4** 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.

**1.5** To preserve his independence from government, the C&AG has complete discretion in carrying out his functions. Responsibility for 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.

### Our work

**1.6** 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. As well as performing financial audits on the accounts of central government departments and other public bodies, the NAO also carries out a range of value-for-money audits, investigations, landscape reviews and good-practice reviews. Our work is always based on evidence.

**1.7** Thanks to our unique public audit perspective, our work has the power to help public servants identify good practice, to help Parliament to enhance its understanding of the practical effects of policy and to help government draw better connections between its decisions.

## Financial audit

**1.8** The C&AG, with the support of the NAO staff, provides an independent audit opinion on some 390 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.

## Wider assurance work

**1.9** Our value-for-money reports examine whether public bodies achieve value for money – efficiency, effectiveness and economy – in their use of resources. Typically, these focus on a specific area of government expenditure and seek to reach a judgement on whether value for money has been achieved. We also make recommendations on where public services can be improved.

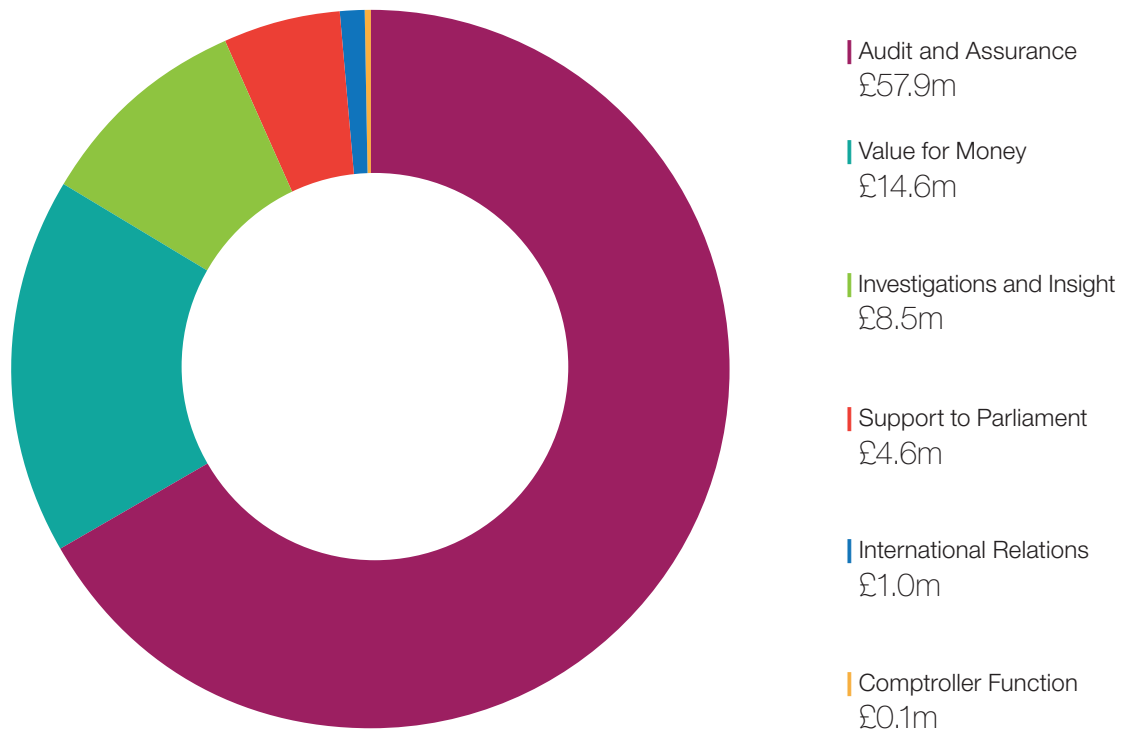
**1.10** In addition to our value-for-money reports, we also carry out a wide range of other work to support Parliament in holding government to account. This includes:

- **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. In particular, we support the Committee of Public Accounts, other select committees and individual MPs in their scrutiny of public spending and delivery. The Committee 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 then typically publishes reports, including recommendations, to which the government must respond in a published Treasury Minute.
- **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,<sup>1</sup> which sets out what local auditors need to do to meet their statutory responsibilities.
- **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 Organization 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 figure below shows the range of our work in 2018-19 and the allocation of resources

The range of our work 2018-19



## Snapshot of our work

**1.11** During 2018-19 we have:

- delivered audit opinions on some 390 accounts across the public sector, including the major government departments;
- published 66 value-for-money and wider assurance outputs;
- supported 61 Committee of Public Accounts evidence sessions;
- responded to 1,054 items of correspondence from the public, provided 152 responses to correspondence from MPs, and responded to 92 enquiries under Freedom of Information; and
- secured the appointment as the external auditor of the World Intellectual Property Organization and the Pan American Health Organization. In addition, the C&AG was elected as chair of the United Nations Panel of External Auditors.

**1.12** Detailed information on our performance is contained in our [Annual Report and Accounts 2018-19](#).

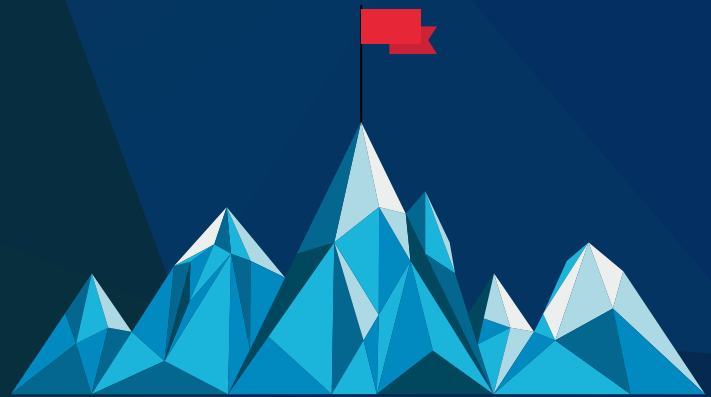
# OUR VALUES

Our values underpin everything we do. We are:



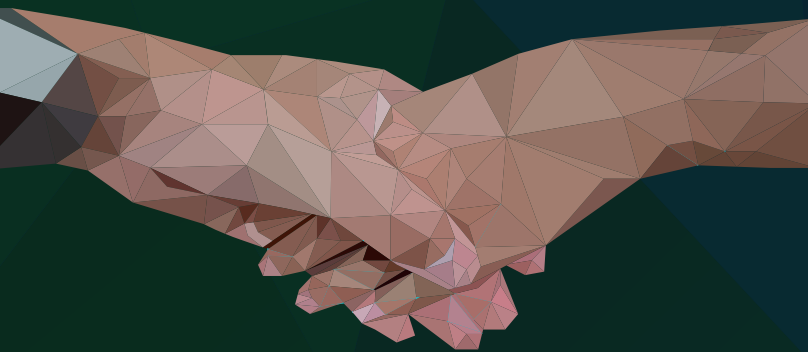
## INDEPENDENT

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.

## Impact of our work

**1.13** 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 [Annual Report and Accounts 2018-19](#) highlights 14 case studies illustrating the wider impact brought about through our work. These wider impact case studies have been approved by the bodies to which they relate.

**1.14** In addition to these case studies, each year, we assess where our work has resulted in an improvement with a financially quantifiable net benefit. The audited bodies concerned confirm these financial impacts and our external auditor gives assurance on them. Between the years 2010 and 2017 we exceeded our financial impact target of £10 for every £1 we spend. During the calendar year 2018, our financial impact was £539 million, which represents around £8 for every pound we spend. A list of financial impacts valued at more than £5 million is included in the NAO’s [Annual Report and Accounts 2018-19](#).

**1.15** The audited impacts in 2018 were less than our target of £10 per every £1 the NAO costs Parliament. One of our biggest impacts results from work we did with the Department for Work & Pensions (DWP). Since 2011 DWP has underpaid Employment and Support Allowance (ESA) due to errors in calculating entitlements. DWP considers that work undertaken in response to our recommendations led it to apply greater scrutiny to overpayments and underpayments, including detailed analysis of ESA underpayments after May 2016. It was this analysis that, ultimately, led to the DWP taking action on the issues covered in our report on ESA underpayments.

**1.16** DWP has recognised the contribution of the NAO and estimates it will pay £920 million (forecast expenditure rounded to the nearest £10 million) in past underpayments over the financial years 2017–2020. In addition, it will pay higher awards to active claimants after their claim is corrected. These amount to around £40 million in 2018-19, £120 million in 2019-20, and then decline over time to £90 million in 2024-25 as claimants leave the benefit. However, these estimates are only finalised once individual cases are reviewed and payments are made.

**1.17** DWP is currently in the process of contacting, reviewing and where necessary correcting the cases of those potentially affected. During the calendar year 2018, which is our cut-off for recording impacts, DWP paid around £285 million in arrears payments and higher awards to cases affected by underpayments on conversion from previous incapacity benefits to ESA. We have included these in our financial impacts performance against target for the year. However, if these estimates of future payments prove to be accurate and we were to include these in our actual performance for the 2018 year, we may have met or exceeded our target.

**1.18** We also monitor our impact by reviewing 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 and Accounts 2018-19](#).

**1.19** An important measure of the quality and impact of our work is how much it helps senior civil servants and chairs of audit committees to drive improvements in public services. We seek feedback on our work through an independently conducted survey and interview programme. We draw on this feedback to support continuous improvement in our practice.

**1.20** In line with the results of the survey in 2017, audited bodies remained satisfied with the NAO. Ninety-seven per cent of survey respondents agreed that their relationship with us was good or very good.

**1.21** Respondents have a high regard for our financial audit work. Ninety per cent agreed it is of high quality; 70% said that our financial audit work brings valuable insights; and 89% said that they would actively seek our feedback on accounting and financial control issues.

**1.22** Of those respondents directly involved in value-for-money studies (41 respondents), a higher proportion were positive about our work than in 2017. Seventy-six per cent rated the technical quality of their most recent value-for-money study as good or very good; 73% agreed that it aligned with their organisation's strategic priorities; and 76% said that it covered the right issues.

**1.23** Overall, 55% of respondents said that our recommendations led to improvements and 73% said that, during our work with them, they had made changes prompted by our engagement.

**1.24** 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.

**1.25** The results of the 2018 survey show that we continue to have a strong reputation among Parliamentarians, being both well-known and respected. Three-quarters of those surveyed felt that they knew the NAO very well or a fair amount. Seventy per cent of those surveyed said that their opinion of the NAO was favourable and almost two-thirds would speak highly of us. This is well above average compared with the public and private organisations measured on the survey.

In response to direct survey questions:

- 83% of MPs surveyed rated us as above average for influencing beneficial changes;
- 83% of MPs surveyed rated us as above average for being authoritative;
- 83% rated us as above average for acting impartially and independently; and
- 78% rated us as above average for acting with honesty and integrity.

## Communicating with our stakeholders

**1.26** We recognise that, in order to influence improvement in the public sector, we must communicate in ways that make it easy for our stakeholders to access and understand our work.

**1.27** New techniques have been introduced to help us do this, such as mini-videos summarising our reports in under two minutes, infographics and publishing every figure from each of our reports on our website so that readers can easily download and share them.

**1.28** We have also developed interactive documents that are easy to read electronically, such as our [newsletter for audit committees](#) and our [Departmental Overviews](#), which summarise each major department's responsibilities, how it spends its money and the key developments of its work.

**1.29** We will continue to listen to our stakeholders and improve how we communicate with them.

# Part Two

## AUDIT INDEPENDENCE AND QUALITY

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

### Independence

**2.1** 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.

**2.2** We expect staff to adhere to the relevant internal and external quality standards for our work. For 2018-19, this includes:

- International Standards on Auditing (ISAs) (UK);
- our standards for value-for-money and other 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).

**2.3** The directors of Financial Audit and Value-for-Money Practice and Quality are responsible for supporting audit teams' compliance with the relevant quality standards for their respective specialisms and for creating a culture of professionalism, rigour and openness to challenge.

**2.4** 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.

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

**2.6** 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 culture

**2.7** Our Framework of Behaviours expands on our values, and provides examples of the way we work in delivering high-quality work and achieving our vision. We use the Framework of Behaviours in recruitment and promotion of staff, as well as objective-setting and performance reviews.

**2.8** We take time to recognise colleagues who have made an outstanding contribution to the office through the annual NAO Awards. Staff can be nominated by anyone in the organisation for recognition in up to eight categories, four of which relate directly to our values, with the remainder relating to the positive impact staff have had on colleagues and audited bodies.

**2.9** Our annual People Survey enables us to listen to the views of colleagues across the office on a range of topics, including understanding of our purpose and strategy, understanding of our values, and their views on the extent to which the Leadership Team and directors lead in line with the values. Issues arising are taken forward in action plans tailored to the needs of individual cluster teams.

**2.10** We recognise that staff well-being is crucial in order for the office to deliver high-quality work in a sustainable manner. We have recently refreshed our diversity and inclusion strategy. 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.

**2.11** We recognise 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 where we know previous interventions have not resulted in sustained improvements.

## Our people

**2.12** We deliver high-quality work because we invest in recruiting, developing and retaining the right calibre of 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 and investigations also trained with us as accountants. We also recruit analysts and senior analysts in many specialist analytical disciplines, including economics, data science, statistics, social research and operational research.

**2.13** Our largest sources of talent are our graduate and school leaver programmes, with 69 people recruited to our graduate scheme and nine to our school leaver scheme in 2018. Last year, 83.4% of our trainees passed the Professional Stage examinations for the Association of Chartered Accountants qualification at the first attempt (in line with the national average) and 94.3% passed the Advanced Stage examinations at the first attempt (significantly above the national average of 85.2%).

**2.14** The professional accountancy training for staff is supplemented by in-house bespoke training. All front-line staff working on audit must attend annual assurance updates and have further training on specific areas, as detailed in paragraphs (2.16 to 2.22).

**2.15** On average, staff undertook 6.3 days of structured training during 2018-19. This includes training in areas of specialist accounting and central government audit.

## Financial audit

**2.16** All financial audit staff have access to a wide range of financial audit training, in addition to an annual assurance update. In 2018-19 we increased the amount of technical training provided at the annual assurance update and enhanced the technical training available throughout the year, particularly making online training available with regards to new accounting standards and mandating that staff complete training in the new lease accounting standard (IFRS 16) using this online resource. We continued 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.

**2.17** We have continued to provide further support and training for newly qualified audit principals and senior analysts taking on a lead role on audit engagements. We have embedded a two-year in-house training programme designed to address the challenges of moving from a three-year training programme into a post-qualification stage. This programme consists of learning and development activities 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

**2.18** 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 provide 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.

**2.19** Courses for trainees include among others:

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

**2.20** 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.

**2.21** We also provide formal one-to-one coaching to any member of staff who wants to develop and improve their performance.

### Other learning and development activities

**2.22** We have completed the rollout of an office-wide training programme called The Way We Work, which aimed at empowering NAO people to deliver their best in line with our business priorities and values. We are now evaluating the effectiveness of the programme. During the reporting year we launched two further talent programmes.

### High-quality performance

**2.23** Financial audit conforms to International Standards on Auditing (UK). Our value-for-money assurance work is more varied, consistent with our value-for-money 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 focused briefings on specific issues. It also includes our programme of investigations. Investigations establish the facts when people or our work identify concerns about the use of public funds. They give a rapid and timely account of a situation or issue.

### Financial audit

**2.24** All our financial audit work must comply 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 Organization for Supreme Audit Institutions (INTOSAI).

**2.25** 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.

**2.26** 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 International Organisation of Supreme Audit institutions (INTOSAI) standard setting groups. These appointments seek to ensure that the public sector perspective is properly reflected in developments within the accounting and auditing profession.

**2.27** 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.

**2.28** 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.

**2.29** 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.

**2.30** 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 audit updates and, where appropriate, incorporate them into further guidance, training and embed them into our methodology.

**2.31** 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 further strengthen 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 where potential improvements to audit quality are set out in Appendix Two: Assurance and control.

**2.32** 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.

**2.33** Our Financial Audit Development Plan (FADP) is our change programme designed at improving and evolving our financial audit practice so our work continues to demonstrate its quality and value. The FADP has three workstreams:

- Addressing the risk: This workstream contains projects that focus on ensuring our methodology recognises and respond appropriately to risks to both the audit opinion and wider public sector finances.
- Modernising our audit: This workstream contains projects that focus on ensuring our audits evolve to take advantage of new technologies and meet external expectations as our client base's use of new technology intensifies.
- Supporting our people: This workstream focuses on supporting and motivating our people to carry out quality audits effectively.

### Value-for-money and investigations

**2.34** 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.

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

**2.36** 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). Our internal cold review process checks adherence with the VfM standards and identifies and disseminates lessons to improve our practice.

## Quality control

### Leadership Team

**2.37** 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.

**2.38** 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.

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

**2.40** The value-for-money executive leaders are the Leadership Team members responsible for value-for-money audit quality, reporting to the C&AG, the wider Leadership Team and the Board as appropriate. The value-for-money executive leaders lead the Value-for-Money Quality Group, which comprises six quality leads and provides oversight over all aspects of quality relating to the NAO's value-for-money and wider assurance work. The C&AG and the value-for-money executive leaders are also supported in their responsibilities by the Director of Value-for-Money Practice and Quality. 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

**2.41** The Practice and Quality Teams consider and report the results of the external monitoring of financial audit and value-for-money and investigations to the C&AG and the Leadership Team. Key findings are shared with colleagues across the financial audit and value-for-money practices. The following paragraphs provide an overview of these arrangements.

#### External monitoring – financial audit

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

**2.43** The AQRT is 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. During 2018-19, the AQRT completed its review of a sample of seven of our 2016-17 financial audits: four Companies Act 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 AQRT is close to completing its review of a sample of seven of our 2017-18 audits and our related wider policies and procedures.

**2.44** Although these samples are small and 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.

**2.45** 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.

**2.46** 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 reports and investigations

**2.47** Each year, external specialists review a sample of published value-for-money reports and investigations. In 2018-19 Oxford Business Schools, Risk Solutions and RAND Europe undertook this work, examining 11 reports. The reviews considered the scope of the report, quantitative and qualitative analysis, structure and presentation, graphs and statistics, methods used, synthesis of conclusions, recommendations (where made), systematic issues and overall perception.

**2.48** The reviewers assessed reports as well structured and well written, with high ratings for how the team set the scope, objectives and managerial context. Reviewers noted some cases where we could have provided more details about our methodology and been clearer how we have judged value for money. Further details of these monitoring arrangements can be found in Appendix Two: Assurance and control.

# Appendix One

## GOVERNANCE AND ACCOUNTABILITY

**1** 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 Comptroller and Auditor General's (C&AG's) independence in giving audit judgements.

**2** 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 Parliament, 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.

**3** 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.

**4** 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.

**5** During 2018-19 our Board members and Leadership Team were as set out on pages 25 to 29.

**6** 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 Board and Leadership Team respectively.

**7** 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.



# The NAO Board and Leadership Team



**Lord (Michael) Bichard KCB**  
Chair of the Board

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 Deputy Speaker of the House of Lords from May 2012 to July 2016. 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 KCB**  
Comptroller and Auditor General  
and member of the Board

Amyas Morse was appointed Comptroller and Auditor General on 1 June 2009, for a fixed, non-renewable term of 10 years. He is the chief executive officer of the NAO and an officer of the House of Commons. 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. He is a non-executive board member of the Royal College of Surgeons.



**Janet Eilbeck**  
Non-executive member of the Board and  
chair of the Audit Committee  
Non-executive dignity-at-work lead<sup>2</sup>

Janet is a chartered accountant with more than 40 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, and chairs two legacy staff pension schemes. She was also chair of the Internal Audit Standards Advisory Board (IASAB), and the independent financial expert for the Department for Education. She has been a non-executive member of the Board and the chair of the NAO's Audit Committee since October 2016.

<sup>2</sup> The role of dignity-at-work (DAW) leads is to support NAO people who experience or witness inappropriate behaviour. Janet Eilbeck represents the formal reporting line for DAW leads into the Board.

**Abdool Kara**

Executive Leader and  
member of the Board

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. He is jointly responsible for the leadership of the NAO's wider assurance workstream.

Abdool brings 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**

Executive Leader and  
member of the Board

Daniel Lambauer joined the NAO in 2009 as a performance measurement expert and helped to establish our local government value-for-money team. Before his appointment to the Leadership Team in April 2017, he led the development of the NAO's value-for-money workstream. Daniel is the executive leader with responsibility for the NAO's strategy and operations. He is jointly responsible for the leadership of the NAO's wider assurance workstream. Before joining the NAO, Daniel worked in a range of sectors, including academia, management consultancy and the civil service.

**Kate Mathers**

Executive Leader and  
member of the Board

Kate Mathers joined the NAO in 2000 and joined the Leadership Team in April 2017 as executive leader with oversight of financial audit. Before her appointment to the Leadership Team, she led the development of the NAO's financial audit practice. Kate is jointly responsible for the leadership of the NAO's financial audit workstream.

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.

**Rebecca Sheeran**

Executive Leader  
Executive dignity-at-work lead<sup>3</sup>

Rebecca Sheeran has worked at the NAO since 2004 and joined the Leadership Team in April 2017 as executive leader with oversight for our value-for-money work in a number of areas. She is a chartered accountant with many years' experience in both financial and value-for-money audit of a range of public sector bodies. Before taking up her post on the Leadership Team, Rebecca directed the NAO's value-for-money audit of the Department for Transport and Network Rail and continues to oversee much of the NAO's work looking at major infrastructure and equipment programmes. Since joining the Leadership Team, she has also overseen the NAO's response to government's preparation for EU exit and is jointly responsible for leadership of the NAO's wider assurance workstream.

**Ray Shostak CBE**

Non-executive member of the Board

Ray Shostak held a number of positions in local and central government, including head of the Prime Minister's Delivery Unit, director of public services in Her Majesty's Treasury and director of Hertfordshire's children, schools and families department. In addition to working internationally with other governments on performance and reform issues, Ray is currently the chair of trustees of the Consortium of Voluntary Adoption Agencies, a trustee of the Early Intervention Foundation, a member of the Public Policy Committee of the British Academy and is an Honorary Norham Fellow at Oxford University. He has been a non-executive member of the Board since January 2015 and chaired the Remuneration and Nominations Committee until January 2018.

**Stephen Smith**

Executive Leader

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 NAO's financial audit workstream, a portfolio of public sector bodies and, more generally, our corporate and financial sector-related work.

<sup>3</sup> The role of dignity-at-work (DAW) leads is to support NAO people who experience or witness inappropriate behaviour. Rebecca Sheeran represents the formal reporting line for DAW leads into the Leadership Team.



**Robert Sykes OBE**

Non-executive member of the Board, senior independent member, member of the Audit Committee, and the Remuneration and Nominations Committee

Robert Sykes 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 public and private sectors and has wide experience of coaching and leadership training. 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 director. 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 second and final three-year term.



**John Thorpe**

Executive Leader

John Thorpe joined the Leadership Team in January 2014. He has had experience across a range of portfolios throughout his NAO career, including employment, agriculture, and international. 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 NAO's financial audit workstream and international work.



**Dame Clare Tickell**

Non-executive member of the Board, and chair of the Remuneration and Nominations Committee

Dame Clare Tickell has extensive experience at board level, having led a variety of organisations across the charitable and public housing sectors. She was chief executive officer of Hanover Housing Association until its merger with Anchor Trust in November 2018, having previously been chief executive of Action for Children. In 2014 she became chair of the Early Intervention Foundation, one of the government's What Works Centres. Dame Clare qualified as a social worker at Bristol University 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; chair of the Community and Voluntary Services Honours Committee from 2011 to 2018 and a former board member of The Guinness Partnership. She is a fellow of the RSA, and chair of the Big Society Trust. From 2011 to 2013, she chaired the Commission on the Future of Hospice Care.

**Max Tse**

Executive Leader  
Executive dignity-at-work lead<sup>4</sup>

## Structure of governance

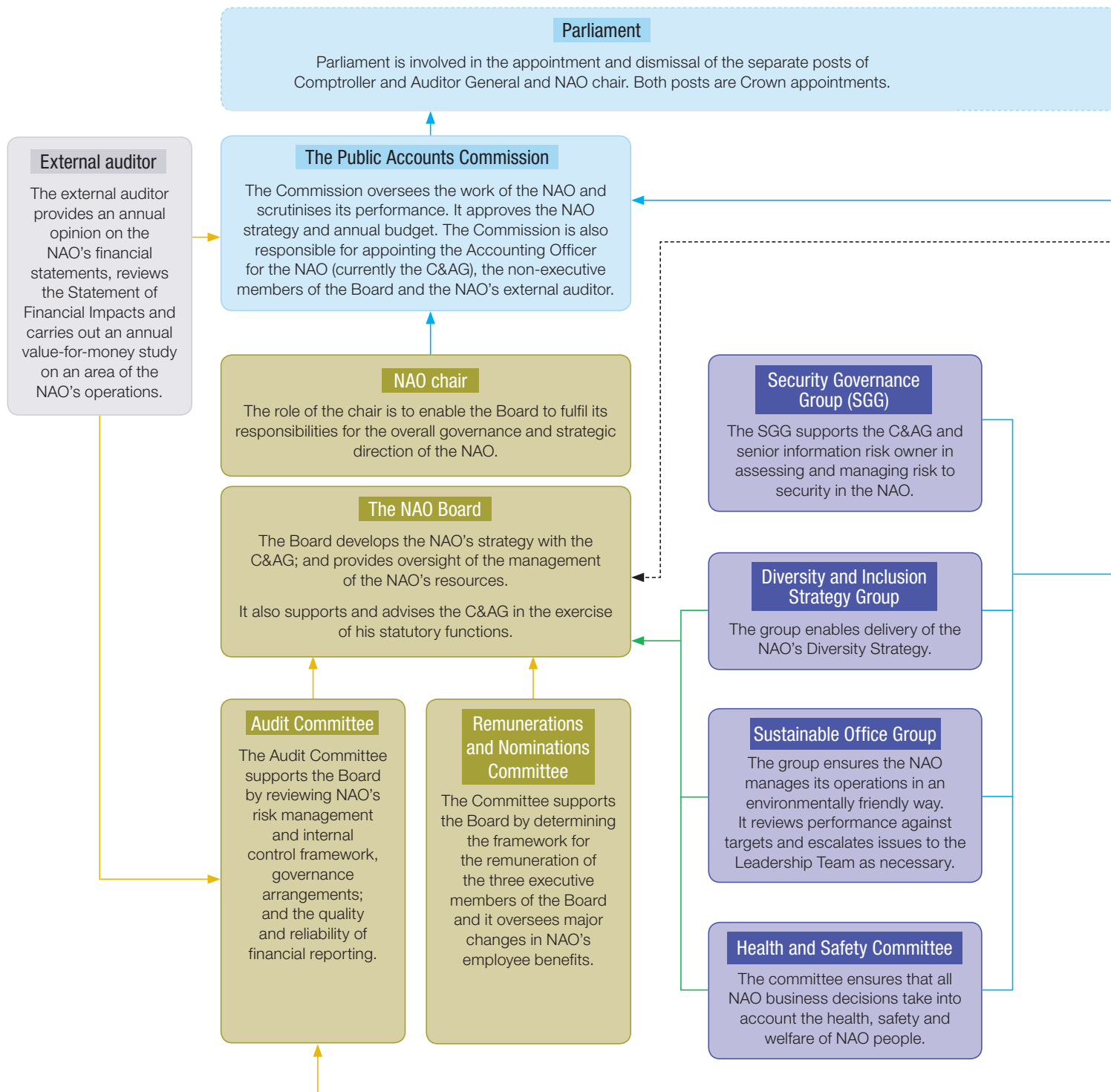
Our governance structure ensures there is proportionate and independent oversight and controls of our own operations, while preserving my independence as the C&AG with respect to audit judgement. The graphic on pages 30 and 31 sets out the NAO's governance framework.

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. He is jointly responsible for the leadership of the NAO's wider assurance work-stream. Before 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.

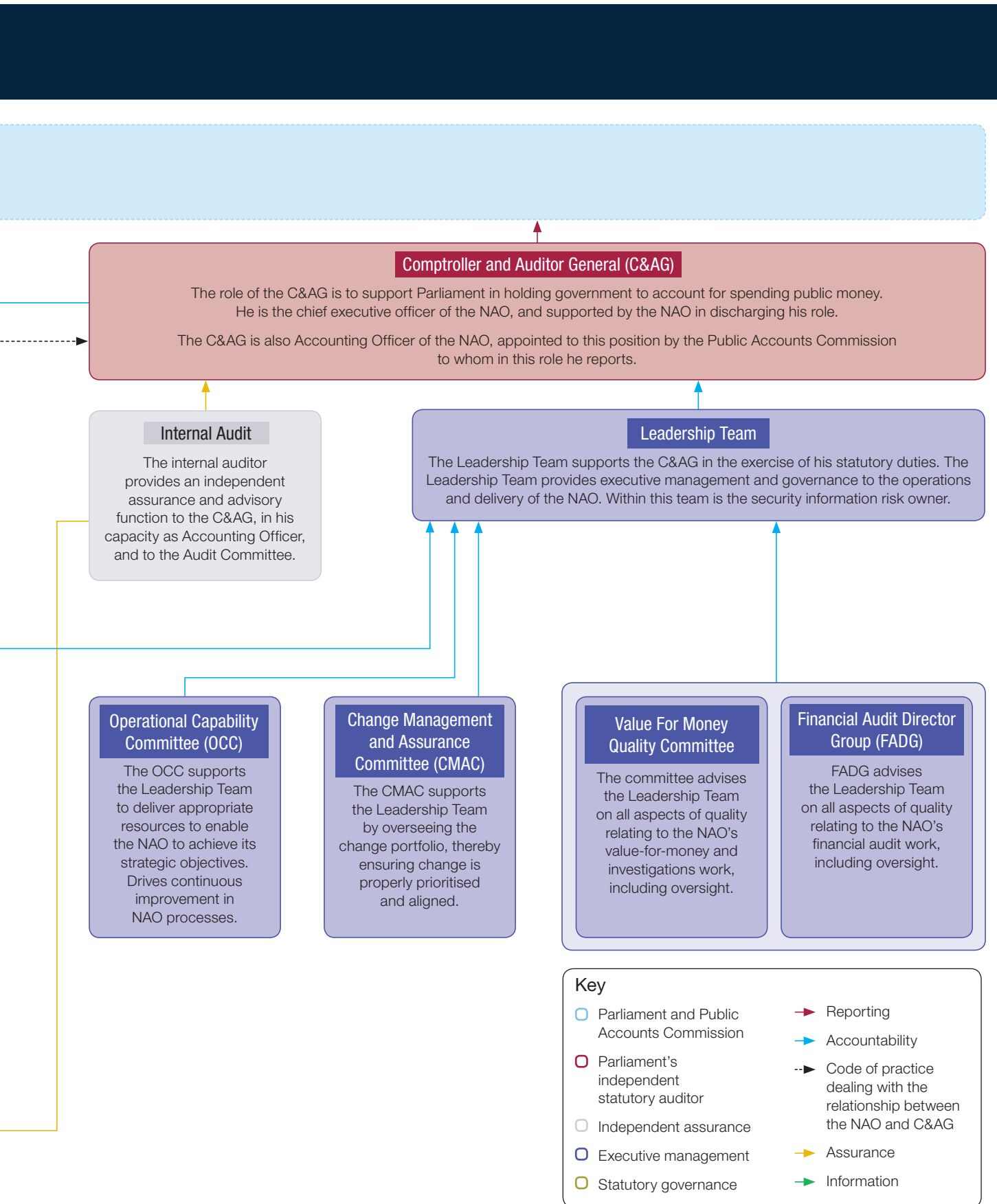
<sup>4</sup> The role of dignity-at-work (DAW) leads is to support NAO people who experience or witness inappropriate behaviour. Max Tse represents the formal reporting line for DAW leads into the Leadership Team.



# NAO governance framework



Source: National Audit Office



**8** 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.

**9** 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.

**10** In 2018-19, the Board met seven times, including one meeting devoted to strategy.

**11** In light of the C&AG's fixed 10-year non-renewable term of office coming to an end on 31 May 2019, the Board agreed a transition plan from one C&AG to the next at its meeting in September 2018. The plan focuses on enabling the next C&AG to discharge the full range of his statutory obligations from day one. The chair of the Board was a member of the selection panel for the recruitment of the next C&AG, together with the chair of the Committee of Public Accounts and the permanent secretary to HM Treasury. The panel was chaired by the chair of the Committee of Public Accounts. On 6 March 2019, the House of Commons approved the motion moved by the Prime Minister to appoint Gareth Davies as the next C&AG from 1 June 2019. The motion was supported by the chair of the Committee of Public Accounts.

**12** During the year, the Board addressed a range of specific issues drawn from our strategy, including our work on Brexit, accountability, audit quality, client feedback and cyber security. The Board also provided feedback on the diversity and inclusion strategy, and the communications strategy. The chair has evaluated the performance of the non-executive members and the chair's performance has been evaluated by the senior independent director. The Board completed a self-assessment of its performance in March 2019 and will discuss areas for improvement with the next C&AG in the autumn.

**13** Our formal governance structure during 2018-19 is shown on pages 30 and 31.

### Review of effectiveness

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



**15** In his 2018-19 annual report to the C&AG, the DIAA concludes that the NAO “has adequate and effective governance, risk and control arrangements”. The DIAA has arrived at this opinion through:

- conducting a detailed risk-based internal audit needs assessment, from which he has prioritised activity over a three-year planning period to design an internal audit strategy and annual operational plan;
- consistently applying a risk-based methodology, which has been validated by an External Quality Assessment in 2017 commissioned by the Audit Committee as conforming to the Public Sector Internal Audit Standards;
- delivery of 29 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 the progress as ‘good’.

**16** The DIAA has assured the C&AG that the resources made available to him have been sufficient to complete his operational plan and the safeguards in place have maintained his independence.

**17** The Board keeps its internal control arrangements under review in response to internal and external developments. The Board is independently advised by the Audit Committee, which met four times during the financial year.

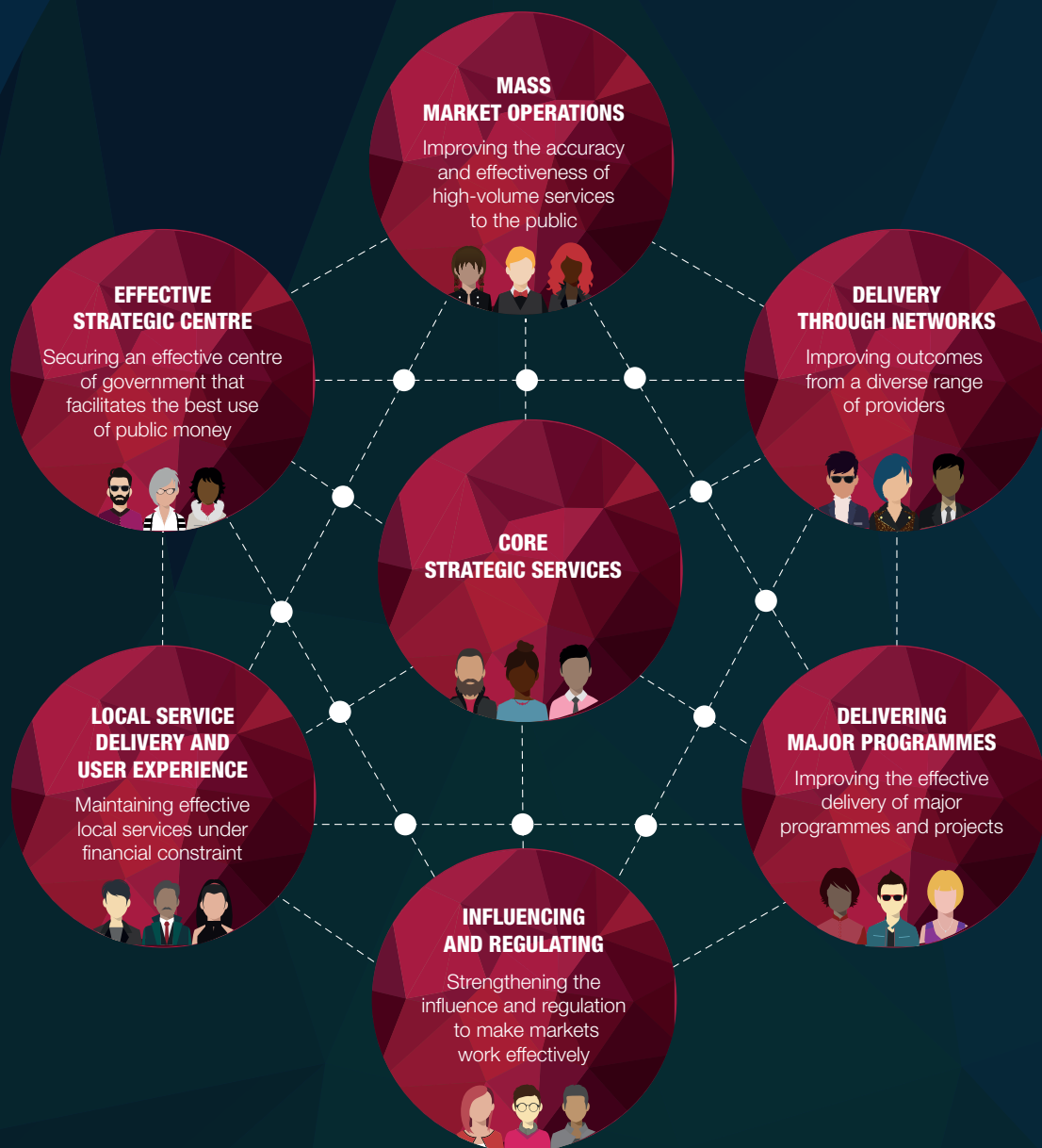
**18** The C&AG is able to report that there were no significant weaknesses in the NAO’s system of internal controls in 2018-19 that affected the achievements of the NAO’s key policies, aims and objectives.

## Structure

**19** We structure our teams into six groups, known as clusters. Each cluster covers departments facing similar issues, such as major infrastructure projects and programmes or complex service delivery. They bring together skills from multiple disciplines to focus our resources where they are needed most. The NAO is supported by a seventh central ‘core strategic services’ cluster, which provides expert advice on the quality of our work and makes sure our internal operations run smoothly.

**20** Each cluster has a management structure comprising a strategy and planning director, a people director and a quality lead director. They are collectively responsible for operationalising our business priorities and developing the NAO’s work programme. Each cluster is held accountable for delivery of the NAO’s business priorities by an executive leader. The clusters, their objectives and strategies, are shown on pages 34 and 35.

# 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.

# Cluster strategies

## Mass Market Operations

The cluster is concerned with how government maintains the efficient and accurate administration of benefits, taxes and pensions. It also looks at the themes of organisational transformation and sustained customer service performance.

## Delivery Through Networks

The cluster considers the effectiveness of the oversight and intervention regimes that departments and other bodies have in place where their objectives are being delivered through other organisations, such as arms-length bodies, charities and commercial entities. The cluster also reviews the services these bodies provide and their accessibility to the public.

## Delivering Major Programmes

Much of the cluster's work focuses on the effective delivery of some of the largest programmes in government. These programmes consume a lot of resource, are inherently risky and are often 'too big to fail'.

## Influencing and Regulating

The cluster's work relates to how government intervenes in, or exercises influence over, markets and complex delivery chains to benefit consumers, the environment, or the wider economy. This cluster focuses on the effectiveness of government's indirect interventions, such as influencing, regulating or subsidising private sector activities, and how government could improve them.

## Local Service Delivery and User Experience

Local government and health services are very important to the public, taxpayers and Parliament. The priority of the cluster is to examine the financial sustainability of these services, along with ensuring the existence of sound systems and accountability and regulation.

## Effective Strategic Centre

The cluster focuses on how well the centre of government works. This includes the preparations for the UK's exit from the EU, alongside its role in securing sustainable public finances and effective accountability for public money.

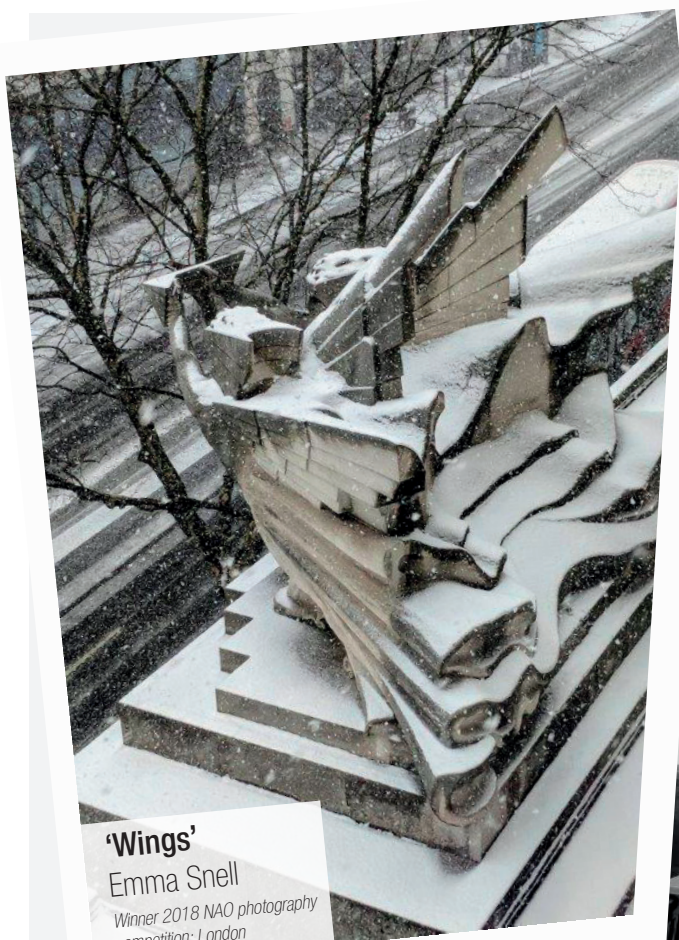
## Core Strategic Services

The cluster is integral to the NAO achieving its objective. It supports the quality of the NAO's audit work and the value it delivers to audited bodies and Parliament. It aims to lead the way in modern, professional management practices and standards, looking to spot 'next practices' and share opportunities to help the NAO improve its ways of working.

## Where we work

**21** We operate across two sites, London and Newcastle. Most NAO staff are based in our London office. The London building is Grade II listed, designed by Albert Lakeman and originally built for Imperial Airways as its 'Empire Terminal'. In 2009 we undertook a significant refurbishment of the building to transform it into a modern, open-plan office. The refurbishment has also enabled the NAO to introduce many environmentally friendly features, such as rainwater harvesting. In 2018-19, following an internal re-organisation, including the implementation of flexible working, we rented out two additional floors to tenants, which reduces the costs of running the NAO for Parliament. We participated in the Open House London event in September 2018, and welcomed 453 members of the public to tour the building.

**22** We have had an office in Newcastle for more than 10 years, which benefits us in terms of our responsibility for a few large audits, such as the Department of Health & Social Care and the Department for Work & Pensions, as well as a number of smaller audits such as the Marine Management Organisation and the Equality and Human Rights Commission. Many of our audits combine both Newcastle and London staff. For example, our value-for-money report examining the Nuclear Decommissioning Authority's progress with reducing risk and hazard at its largest and most hazardous site, Sellafield, comprised a team of financial auditors, analysts and value-for-money experts from both offices.



**'Wings'**

Emma Snell

Winner 2018 NAO photography  
competition: London



**'Tyne Bridge'**

Simon Wakefield

Winner 2018 NAO photography  
competition: Newcastle

## People

**23** We publish an organisation chart showing our structure and leadership's responsibilities on our website.

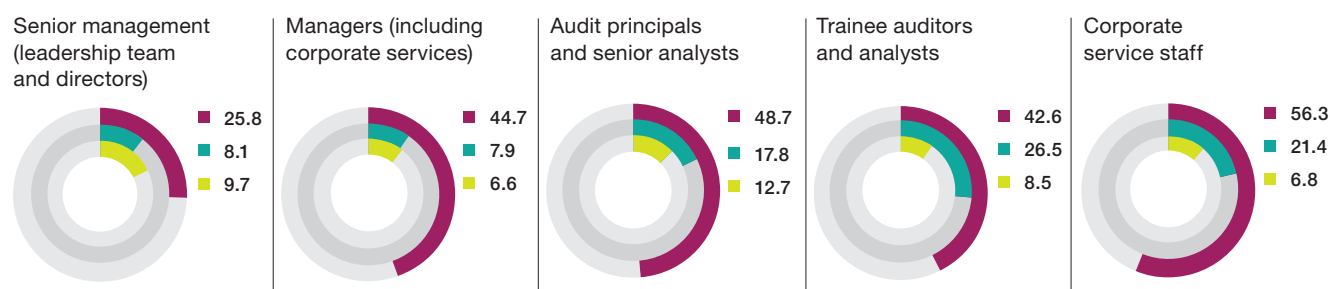
**24** Staff composition as at 31 March 2019 and the staff distribution by grade and diversity for all staff in post is set out below.

### Staff composition as at 31 March 2019

#### Average number of persons employed

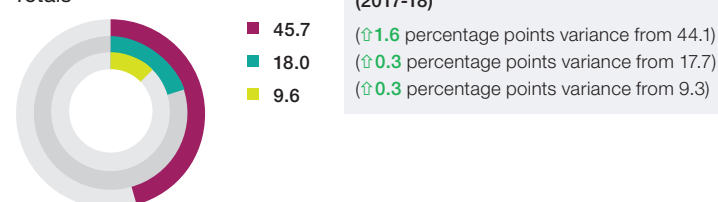
	2018-19	2017-18	2016
Full-time equivalent permanent staff	806	806	806
Inward secondees	2	3	3
Temporary staff	18	5	5
<b>Total</b>	<b>826</b>	<b>814</b>	<b>814</b>

#### Grade diversity as at 31 March 2019 (%)



Percentage shown out of 100.

#### Totals



#### (2017-18)

(↑1.6 percentage points variance from 44.1)  
 (↑0.3 percentage points variance from 17.7)  
 (↑0.3 percentage points variance from 9.3)

#### Key

- Women
- Black, Asian and Minority Ethnic (BAME)
- Disabled

#### Note

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

Source: National Audit Office



**25** As at 31 March 2019, the proportion of women above manager level was 25.8%, a decline on the previous year. We have faced challenges in improving the gender diversity of staff at more senior levels, including fewer female applicants for promotion to director.

**26** Encouragingly, there has been an increase in the proportion of women employed across the NAO, including in the feeder grades to director. We continue to focus on establishing a diverse trainee base, taking action to improve equality in our trainee selection process and building on the actions taken in 2018-19. Our new Diversity and Inclusion (D&I) strategy provides further impetus to improve the progression of women to senior grades.

**27** Representation of Black, Asian and minority ethnic (BAME) colleagues within the NAO as a whole has remained unchanged against the previous year, at 18%. Representation has, however, increased marginally in grades at manager and above. We remain focused on improving our ethnic diversity at all levels and have started to explore how we can better support the progression of BAME colleagues through sponsorship and mentoring programmes.

**28** Over the past three years, 9% of the graduates we have recruited have had a declared disability, which is significantly higher than the intakes of the majority of graduate employers. However, we continue to explore how we might better market our offer to disabled candidates. We are focusing on improving the workplace experience of disabled colleagues, ensuring we are making effective adjustments and building line managers' confidence in managing colleagues with a disability. Having achieved level 2 of the disability confidence scheme, we are now working towards level 3 accreditation.

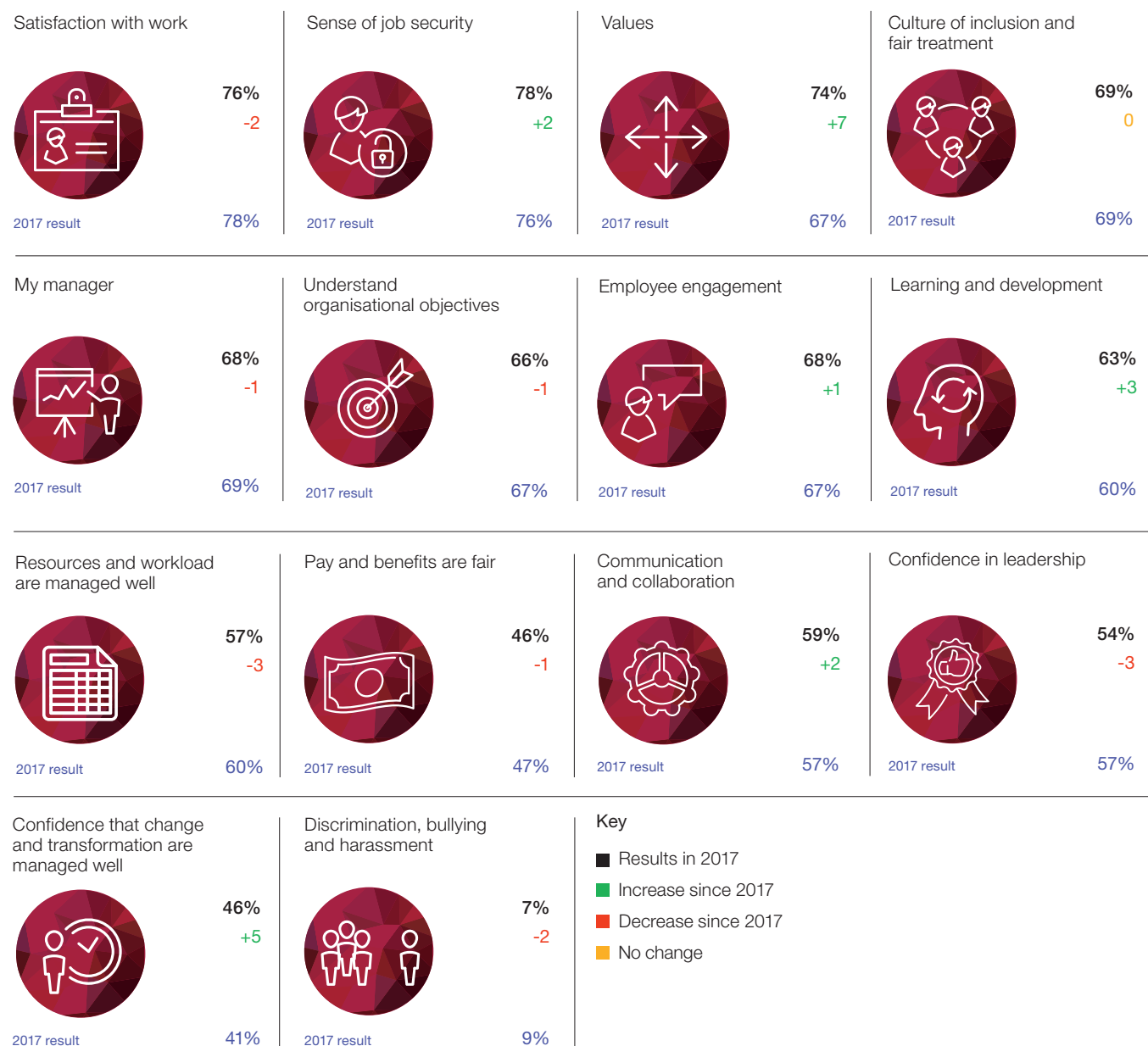
### Staff survey

**29** We conduct an annual survey of our people and benchmark the results against comparable organisations. In 2018, 77% of NAO staff completed the annual survey, which was the same percentage as 2017. We are pleased that the results continue to show strong levels of employee engagement within the NAO, which compare favourably with our benchmarks. Employee engagement, at 14% higher than the civil service average, reflects our people's pride and motivation at working at the NAO

**30** We have worked hard to improve how we support and engage our people through creating a more flexible environment, implementing more modern systems and developing our ways of working. However, we want to continuously improve what we do and ensure that we keep up to date with best practice for engaging the modern workforce. Our continued areas of focus in the coming year will be: to improve our workforce planning and peak workload management, develop and implement a new internal communication strategy and developing how our leaders engage with our people.

## National Audit Office People Survey results, by topic areas

### Results of the survey in 2018 compared with 2017



#### 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 14 broad topic areas covered in the survey.

Source: National Audit Office

## Financial information

**31** Each year, the NAO's external auditor undertakes an annual value-for-money review of a specific aspect of the NAO's business. In 2018 the topic for review was NAO's contract management. The conclusion the external auditor has drawn is positive overall. The review makes five recommendations for improvement, which management is taking forward.

**32** The report was submitted to the Public Accounts Commission in December 2018 and can be found on the [Commission's website](#).

**33** Our full financial information is contained in our *Annual Report and Accounts 2018-19*, which can be found on our link to the report. 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 67 per cent of NAO's gross expenditure. The remainder relates to other assurance work. The C&AG's Comptroller function is reported as a separate segment.

	2018-19								
	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	57,864	14,600	8,507	4,633	1,024	119	86,747	296	87,043
Income from services provided	(18,478)	–	–	–	(410)	–	(18,888)	–	(18,888)
Rental and other income	(1,451)	(366)	(213)	(116)	(26)	(3)	(2,175)	–	(2,175)
<b>Net expenditure</b>	<b>37,935</b>	<b>14,234</b>	<b>8,294</b>	<b>4,517</b>	<b>588</b>	<b>116</b>	<b>65,684</b>	<b>296</b>	<b>65,980</b>

### Notes

- 1 The NAO reports expenditure and income under six operating segments, further information about which can be found on page 11. Non-voted expenditure comprises the C&AG's and Chairman's salaries and is paid directly from the Consolidated Fund, which is outside of the control of the NAO.
- 2 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 work. Rental income cannot be directly attributed to the NAO's operating segments and has been apportioned in line with gross expenditure.
- 3 We consider the chief operating decision body of the NAO to be the Leadership Team, details of its membership can be found on pages 25 to 29. 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.



**34** Our *Annual Report and Accounts 2018-19* 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.

**35** 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.

# 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 2018-19.

**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.

## 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

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

### Second stage review

**8** 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.

**9** 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.

**10** 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 relevant experienced senior National Audit Office (NAO) staff the director considers appropriate.

**11** 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.

**12** Our internal Compliance and Quality Unit (CQU) oversees a programme of reviews of audit files supporting 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; and
- the quality of evidence the team collected to support the audit.

## Audit licences

**13** 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 general audit licences to all staff who:

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

**14** The director of Financial Audit Practice and Quality oversees the arrangements for allocating licences to staff whose work involves complex IT systems, and 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.

**15** 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.

## Value-for-money and investigations

**16** 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 12 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.

**17** The VfM standards are underpinned by core policies and procedures that 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.

### Control framework

**18** Directors ensure that there are proportionate and appropriate quality assurance arrangements for their studies and investigations. For each study there is a quality assurance plan, which is agreed by an independent director within the cluster. 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, advised by the Leadership Team, selects 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 arrangements 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 a sample of publications each year, from across the office and from our full range of wider assurance products. We identify (using a standard set of criteria) and examine any risks to quality and/or compliance with the VfM standards. Thirteen outputs published in 2018-19 have been subject to an internal cold review. Not all reviews have been completed at the time of publication of this *Transparency Report*. For the publications for which reviews have been completed, the reviews highlighted some common issues including: consistency in documenting audit evidence; and compliance with mandatory steps for documenting director review.
- External cold review: a sample of published outputs (11 in 2018-19) are subject to an independent, external review. The reviewer considers the report against a set of agreed criteria.

## External monitoring

### External review – financial audit

**19** The Audit Quality Review Team (AQRT) of the Financial Reporting Council reviews a selection of our audit files and carries out a cyclical review of the NAO's processes, policies and procedures supporting audit quality.

**20** During 2018-19, the AQRT completed its review of seven 2016-17 audit files (prior year: six), of which four (prior year: two) were performed under the Companies Act 2006. It was also close to completing its inspections of a sample of seven of our 2017-18 audit files.

**21** During 2018-19, we responded to the AQRT's reviews of a sample of our 2016-17 audits. We:

- communicated the AQRT's findings to all staff and incorporated the feedback into our financial audit update training in autumn 2018;
- 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;
- 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 CQU and redesigned the internal review programme.

**22** Additionally, we have:

- dedicated more senior staff across our audit practice and highest risk audits;
- enhanced the guidance in place over audits undertaken under contracted-out arrangements;
- introduced updated EQCR guidance, checklists and training to focus on key matters. estimates, management judgements, and key audit documentation; and
- established centres of expertise for the audit of fraud and error to share knowledge and facilitate appropriate challenge and continuing to develop centres of expertise for the audit of pensions, property and estimates.

**23** At the time of publication of this *Transparency Report*, the AQRT review of our 2017-18 audits is close to completion. The AQRT recognised the NAO's continuing work to enhance the policies and procedures supporting and promoting audit quality. Examples include addressing lessons learned from previous AQRT individual review reports, improving the scope and coverage of our own internal cold reviews, and identifying thematic issues so that these are more effectively embedded within individual audits.

**24** On individual inspections, key emerging findings are for us to:

- improve the extent of challenge and ensure that sufficient audit evidence is obtained in areas of judgement, in particular for key assumptions used in valuations and estimates;
- ensure substantive testing procedures are appropriate to provide a sufficient level of audit evidence in relation to revenue and inventory;
- continue to review internal guidance for group audits, including how the group audit team evidences its direction, oversight and review of component auditors;
- improve the testing of controls and ensure that any weaknesses are compensated by enhanced substantive testing; and
- continue to perform root cause analysis on the key findings of the audits reviewed.

**25** We have already started to respond to these emerging findings, and will develop a plan to monitor the progress of agreed actions. For example, we communicated these findings to all staff through a Financial Audit Bulletin in March 2019, and included the findings as a key component of our mandatory financial audit update courses in April 2019.

**26** We continue 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 also have 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 reports and investigations

**27** For more than two decades we have used external specialists to review value-for-money reports. In 2018-19, a sample of 11 reports were reviewed by independent experts from Oxford Business Schools, Risk Solutions and RAND Europe.

**28** 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.

**29** They provide a written review assessing how each report performs against the criteria in (paragraph 28) above, including an overall assessment. The Value-for-Money Quality Group uses these reviews as the basis of discussions on quality.

**30** 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 the disclosures required by Article 13 of Regulation (EU) No 537/2014 and how the National Audit Office (NAO) complies with these disclosures.

Provision of Regulation (EU) 537/2014	How the National Audit Office (NAO) complies with Regulation (EU) 537/2014
A description of the legal structure and ownership of the audit firm.	The Comptroller and Auditor General (C&AG), Sir Amyas Morse, leads the NAO and is an officer of the House of Commons, as established by statute. He and the staff of the NAO (about 800 people) are independent of government. They are not civil servants and do not report to a minister.  See also Appendix One: Governance and accountability.
Where the statutory auditor or the audit firm is a member of a network:	N/a. The NAO is a Supreme Audit Institution and not part of a network.
<ul style="list-style-type: none"> <li>i a description of the network and the legal and structural arrangements in the network;</li> <li>ii the name of each statutory auditor operating as a sole practitioner or audit firm that is a member of the network;</li> <li>iii the countries in which each statutory auditor operating as a sole practitioner or audit firm that is a member of the network is qualified as a statutory auditor or has his, her or its registered office, central administration or principal place of business;</li> <li>iv the total turnover achieved by the statutory auditors operating as sole practitioners and audit firms that are members of the network, resulting from the statutory audit of annual and consolidated financial statements.</li> </ul>	
A description of the governance structure of the audit firm.	The NAO's governance structure is shown in Appendix One: Governance and accountability.
A description of the internal quality control system of the statutory auditor or of the audit firm 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.
An indication of when the last quality assurance review referred to in Article 26 of Regulation (EU) 537/2014 was carried out.	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 for which the statutory auditor or audit firm carried out statutory audits in the preceding financial year.	<p>In 2018-19, the NAO audited five public interest entities.</p> <ul style="list-style-type: none"> <li><b>1</b> Network Rail Infrastructure Finance PLC</li> <li><b>2</b> CTRL Section 1 Finance PLC</li> <li><b>3</b> LCR Finance PLC</li> <li><b>4</b> NRAM Limited</li> <li><b>5</b> HM Treasury UK Sovereign SUKUK PLC</li> </ul>

A statement concerning the statutory auditor's or the audit firm's independence practices which also confirms that an internal review of independence compliance 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 2018-19.
A statement on the policy followed by the statutory auditor concerning the continuing education of statutory auditors referred to in Article 13 of Directive 2006/43/EC.	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.
Information concerning the basis for the partners' remuneration in audit firms.	The NAO is not an audit firm and has no partners. For details of remuneration, see Appendix One: Governance and accountability
A description of the statutory auditor's or the audit firm's policy concerning the rotation of key audit partners and staff in accordance with Article 17(7) of Regulation (EU) 537/2014.	Directors are rotated at least every five years, and are required to ensure that other team members are not involved in an engagement for more than seven years.
Where not disclosed in its financial statements within the meaning of Article 4(2) of Directive 2013/34/EU, information about the total turnover of the statutory auditor or the audit firm, divided into the following categories:	
<b>i</b> revenues from the statutory audit of annual and consolidated financial statements of public interest entities and entities belonging to a group of undertakings whose parent undertaking is a public interest entity;	<b>i</b> £0.2 million
<b>ii</b> revenues from the statutory audit of annual and consolidated financial statements of other entities;	<b>ii</b> £18.8 million
<b>iii</b> revenues from permitted non-audit services to entities that are audited by the statutory auditor or the audit firm; and	<b>iii</b> The NAO does not carry out non-audit services. The NAO rents office space within its London headquarters (or London building) to three audited bodies. Total rent and service charge income for these bodies: £0.9 million (of a total £2.2 million rent and service charge income). See page 40.
<b>iv</b> revenues from non-audit services to other entities.	<b>iv</b> See <b>iii</b>

Source: National Audit Office

# Appendix Four

## REVIEW OF NAO COMPLIANCE WITH THE AUDIT FIRM GOVERNANCE CODE (REVISED 2016)

- 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 below (pages 51 to 57) 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 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 <i>Annual Report and Accounts</i>
	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.	See <i>Annual Report and Accounts</i> , Structure of Governance section (pages 60 to 64)
	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.	See <i>Annual Report and Accounts</i> , Governance Statement (pages 52 to 57). Meeting attendance record is noted on page 62 of the <i>Annual Report and Accounts</i> .
	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.	The NAO carried out a review of governance in 2018. See <i>Annual Report and Accounts</i> (page 64). The C&AG is appointed for a fixed, non-renewable term of 10 years. Board members are appointed for a three-year term, renewable for one further three-year term. Executive members of the Board are appointed each year, renewable annually.
	A.2: Management principle – A firm should have effective management which has responsibility and clear authority for running the firm.	<a href="#"><u>The Budget Responsibility and National Audit Act 2011 (Part 2, Schedules 2 and 3)</u></a> makes provision for a C&AG, and NAO. We comply fully with requirements. The management team's terms of reference are set out in the NAO's annual report and in this <i>Transparency Report</i> , available on our website.
	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.	See A:2 above. We are considering enhancements to our external website to reflect the arrival of a new C&AG from 1 June 2019. We will consider provision A.2.1 as part of this web enhancement exercise.

**B – Values**

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* and the [NAO Strategy](#), available on our website. Our values are set out on page 12 and paragraphs 2.7 to 2.11 of the *Transparency Report*.

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 Accounts \(page 12\)](#) and the [NAO Strategy](#).

**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.

Please see the Governance Statement (page 52 of the *Annual Report and Accounts*) for details of independent non-executives, and their significant, relevant experiences. 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. The NAO has disclosed information about independent non-executives on its website here: NAO Board and Leadership Team, including [terms of reference for the Board](#). The Board is supported by the [Audit Committee](#) and the [Remuneration and Nominations Committee](#) (terms of reference as linked).

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.

See C.1

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	See C.1
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.	See C.1
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 the NAO's unique statutory position.
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.	These provisions are set out in Schedule 2, Part 2 of Budget Responsibility and National Audit Act 2011. We comply fully. The chair of the NAO may resign by giving written notice to the Prime Minister, and any other non-executive member by giving written notice to the Public Accounts Commission. In respect of right of access to relevant information, this is covered in the Board Terms of Reference as linked in C.1 (Appendix One, page 14).
C.3.1: Each independent non-executive should have a contract for services setting out their rights and duties	We comply fully with this provision.
C.3.2: The firm should ensure that appropriate indemnity insurance is in place in respect of legal action against any independent non-executive.	Indemnification of independent non-executives is covered by <a href="#">section 24 of the Budget Responsibility and National Audit Act 2011</a> .
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.	Included in the senior independent director's role is their duty to act as a mediator between independent non-executives and management.  We provide sufficient resources to the independent non-executives to undertake their duties.
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.	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&AG to determine the most appropriate course of action consistent with his independent statutory role and status. We make this disclosure in this <i>Transparency Report</i> which is published on our website.

**D – Operations**

D.1: Compliance principle – A firm should comply with professional standards and applicable legal and regulatory requirements.

These provisions are covered in Part Two, Quality control.

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.

The *NAO Financial Audit Manual* sets out our audit methodology, which ensures compliance with legal and regulatory requirements, and relevant standards.

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.

See Appendix Two: Assurance and control: Audit licences.

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.

The [Code of Conduct](#) requires all staff to complete an annual declaration of interests via the Code of Conduct and confirm how any conflicts of interest have been managed. All NAO staff are required to notify the relevant engagement director and Human Resources of any possible conflict of interest as soon as it becomes apparent during the course of the year.

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.

See Part Two, External review – financial audit.

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.

These provisions are covered in Appendix One: Governance and accountability.

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.

See Appendix One, paragraph 16.

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.

See Appendix One, paragraph 16.

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.

The director of Internal Audit and Assurance, who advises the C&AG and the Board on the adequacy of the framework of internal controls, uses a 'three lines of defence' assurance model. The C&AG's review of effectiveness as set out in the Annual report and accounts 2018-19 is also informed by the work of the NAO's executive leaders who are responsible for developing and maintaining the internal control framework, and comments made by the external auditors in their management letter.

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.

These provisions are covered in Part Two, Quality control – Our people section, as well as the NAO Annual Report published on our website.

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.

The NAO does not need to publicly commit to the Audit Firm Governance Code due to the NAO's unique statutory position.

The *Transparency Report* contains relevant details and is published on our website.

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

Independent non-executives are involved in this review through the [Remuneration and Nominations Committee](#).

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.

These provisions are covered in our Code of Conduct.

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 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.

Members of the governance structures have been 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.	See E.2
E.2.2: The firm should report that it is a going concern, with supporting assumptions or qualifications as necessary.	See E.2
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.	See E.2
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.	See E.2
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 <i>Transparency Report</i> 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.	See E.4
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.	See E.2
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 <a href="#">here</a> , including membership. The Committee publishes a short description of how it has discharged its duties in the <i>Annual report and accounts</i> .

## 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.	<p>The NAO conducts regular meetings with senior management and we undertake internal and external dialogue.</p> <p>The NAO does not need to publicly commit to the Audit Firm Governance Code due to the NAO's unique statutory position.</p>
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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.

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

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

See F.1

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.

See F.1

Source: National Audit Office



National Audit Office