



National Audit Office

Transparency Report **2021-22**

September 2022

We are the UK's independent public spending watchdog.

We support Parliament in holding government to account and we help improve public services through our high-quality audits.

The National Audit Office (NAO) scrutinises public spending for Parliament and is independent of government and the civil service. We help Parliament hold government to account and we use our insights to help people who manage and govern public bodies improve public services.

The Comptroller and Auditor General (C&AG), Gareth Davies, is an Officer of the House of Commons and leads the NAO. We audit the financial accounts of departments and other public bodies. We also examine and report on the value for money of how public money has been spent.

In 2021, the NAO's work led to a positive financial impact through reduced costs, improved service delivery, or other benefits to citizens, of £874 million.

**National Audit Office
Transparency Report 2021-22**

Gareth Davies
Comptroller and Auditor General
National Audit Office

30 September 2022

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

If you need a version of this report in an alternative format for accessibility reasons, or any of the figures in a different format, contact the NAO at enquiries@nao.org.uk

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2021-22 OUR YEAR IN HIGHLIGHTS

As the UK's independent public spending watchdog, we help to improve public services through our high-quality audits.

We have:

supported Parliament in holding government to account



400

audited accounts published



58

value-for-money reports and investigations published



69

Committee of Public Accounts sessions supported

90%

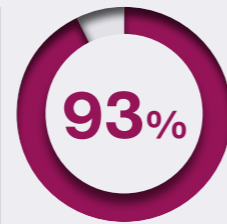
of surveyed MPs agreed we were effective at supporting Parliament in holding government to account and scrutinising public services

encouraged government to learn and embed lessons

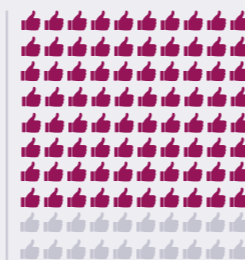


5

lessons learned reports published



of the recommendations we made between 1 April 2019 and 31 March 2021 have been accepted or partially accepted by government, and details published in our recommendations tracker



80%

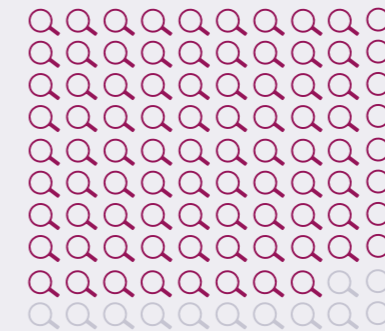
of surveyed senior officials in the bodies we audit agreed that our work leads to better outcomes

used our expertise across financial audit, value-for-money and wider assurance work to draw out impactful insights



8

good practice guidance reports published



88%

of the surveyed senior officials in the bodies we audit agreed we provide insight

had impact and made progress in other areas of our work and organisation



£11

of positive financial impact from our work for every £1 spent



1.7

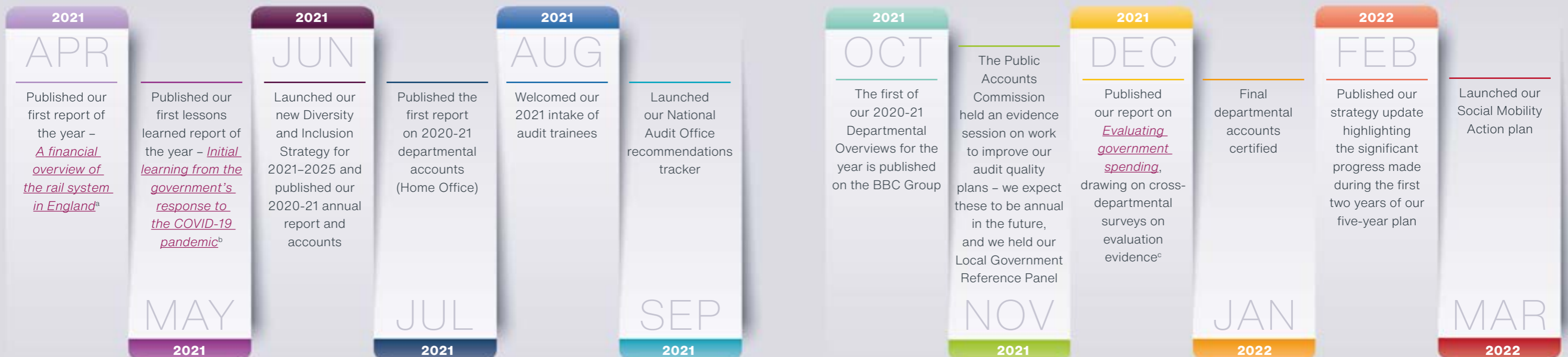
percentage points reduction in our mean gender pay gap, indicating progress with our Diversity and Inclusion Strategy and diversity pay gap



712 tonnes

a reduction to 712 tonnes of carbon emissions from electricity and gas, compared with 770 tonnes in 2020-21

What our year has looked like:

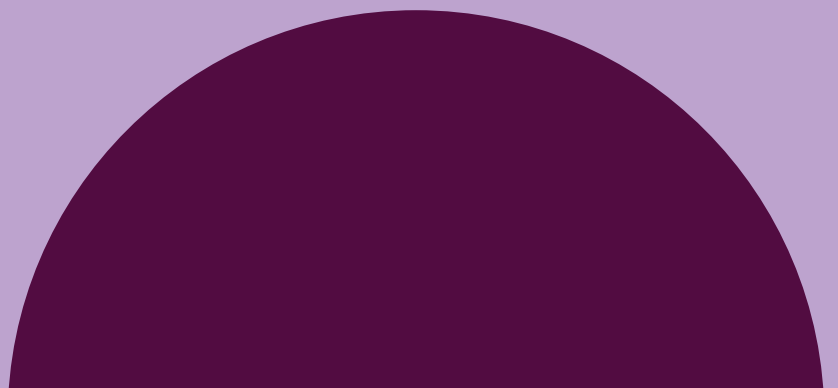


^a Comptroller and Auditor General, *A financial overview of the rail system in England*, Session 2019–2021, HC 1373, National Audit Office, April 2021. Available at: www.nao.org.uk/report/a-financial-overview-of-the-rail-system-in-england/

^b Comptroller and Auditor General, *Initial learning from the government's response to the COVID-19 pandemic*, Session, 2021-22, HC 66, National Audit Office, May 2021. Available at: www.nao.org.uk/report/initial-learning-from-the-governments-response-to-the-covid-19-pandemic/

^c Comptroller and Auditor General, *Evaluating government spending*, Session 2021-22, HC 860, National Audit Office, December 2021. Available at: www.nao.org.uk/report/evaluating-government-spending/

Leadership messages



Foreword from the Comptroller and Auditor General (C&AG)



Welcome to the 2022 National Audit Office (NAO) Transparency Report. This report explains the role we play as the UK's spending watchdog and how we support Parliament in holding government to account through our statutory public audits.

It highlights the governance and management arrangements in place which support the delivery of high-quality financial and value-for-money audit work. It also sets out how we have responded to feedback from internal and external inspections of our work.

Our audits of the 2020-21 accounts of government departments and public bodies needed to respond to the exceptional audit risks arising from government's spending on the COVID-19 pandemic response. The Public Accounts Commission approved additional resources which allowed us to strengthen the audit teams most affected, invest in quality, and deliver the required audit coverage of hundreds of billions in unplanned spending. My reports on the accounts of the Department of Health & Social Care and the Department for Business, Energy & Industrial Strategy illustrate the scale of the audit work required and the extraordinary nature of the sums spent, written-down or provided for.

The pandemic also disrupted the timetables for completing and auditing some accounts. We completed 55% of audits (including six major government departments) by the 2021 summer recess and 53% (including nine major government departments) in 2022. We have a two-year plan for restoring 80% of audits (including all government departments) to this timetable by summer 2024, which would represent a return to the pre-pandemic position.

The quality of our financial audit and value-for-money work is at the heart of what we do. The feedback we have had from our key stakeholders continues to tell us that we are delivering valuable assurance and insights to the bodies we audit and to those who hold these bodies to account.

Our 2021-22 value-for-money (VfM) programme continued to cover the government's response to COVID-19 while also reporting on other important areas of value-for-money risk. In line with our five-year strategy, we have continued to extract the learning from our work across government and present it in the form of thematic reports and good practice guides.

continued >

Foreword from the Comptroller and Auditor General (C&AG) *continued*

We are investing heavily in audit quality. Our Financial Audit Quality Plan recognises that quality comes from clear leadership, a culture of learning and the pursuit of excellence, effective training and development, strong technical resources, effective systems and the retention and recruitment of high-quality professionals.

The Quality Plan responds to the findings of internal and external reviews. In 2021-22, this has included strengthening our Centre of Expertise on Financial Instruments; rolling out mandatory training on key areas of improvement; and sharing the results of root cause analysis so that the learning is applied consistently across our audits. The latest results of external inspections of our audits show that we have addressed some but not all of the areas for improvement previously identified. We continue to focus our efforts on the remaining areas for improvement, in particular our work on complex financial instruments and our reliance on experts when gaining assurance on estimates requiring specialist professional knowledge.

Alongside this improvement activity, we have developed a new audit methodology designed to be compliant with the requirements of the new ISA 315, which sets new standards for risk assessment and planning the audit procedures necessary to address the risks identified. Having piloted the methodology on a sample of 2021-22 audits, we are rolling it out to all audits for 2022-23, supported by a major programme of training for our audit teams.

The next stage in our audit transformation programme is to pilot and then implement a replacement for our audit software platform. The new software is designed to guide auditors to deliver consistently high quality in line with the new methodology and support them in making greater use of data analytics.

I am encouraged by our continuing progress in developing an open culture of improvement, which is fundamental to audit quality. We have been greatly assisted in our quality improvement work by the Audit Quality Board chaired by Janet Eilbeck, which has provided constructive challenge and support on this agenda since it first met in March 2021.

This report provides more details on all these developments. I am hugely grateful to my colleagues for maintaining our drive to improve quality while responding so effectively to the audit challenges presented by the pandemic.



Elaine Lewis

Executive Director responsible for Financial Audit quality, and

Kate Mathers

Executive Director responsible for the Financial Audit service line

We audit an increasingly complex and challenging portfolio of financial statements. This was amplified during 2020-21 by the need to respond to the exceptional audit risks arising from the UK government's unplanned spending on the COVID-19 pandemic response.

Against this background, audit quality is our top priority. We are committed to ensuring that all our work meets our quality standards and we are focused on ensuring that the significant investment we are making continues to have a positive impact on the quality of our financial audit work. Therefore, we are disappointed that the latest findings from our external quality review show that we have more to do to consistently achieve high-quality work and to keep pace with the rising quality bar for the audit profession.

The steps we are taking to achieve this are set out in our Financial Audit Quality Plan. We are confident that our Quality Plan addresses the right areas in the right way, and we will continue to focus on implementing and embedding it across our audits and updating our Plan regularly.

Our Quality Plan takes a whole-system approach. At its heart lie our values, which encourage a culture of transparency, where we are open in discussing quality findings and learning from them.

Key initiatives include significant investment in our Financial Instruments Centre of Expertise and our Audit Transformation Programme.

Our Financial Instruments Centre of Expertise aims to enable us to keep pace more effectively with good-practice expectations and to respond to quality review findings on our work in this complex area.

Our Audit Transformation Programme is a once in a generation investment in our audit methodology and the technology we use to deliver this. We are taking an incremental approach, which over the coming years will transform how we audit, improving quality, insight and efficiency. Each phase of our transformation is supported by significant training and supported development for our auditors. In 2022 we are taking the first major step in our transformation with the roll-out of our new audit methodology.

We look forward to reporting progress in our next Transparency Report.



Rebecca Sheeran

Executive Director responsible for Value-for-Money service line

Our VfM work must meet a consistently high standard to maintain trust, hold government to account and to influence positive changes in public services. We have continued to deliver impactful VfM and wider assurance work that largely meets our high standards. This is a significant achievement in a year in which we have worked rapidly to audit government's response to the COVID-19 pandemic while expanding the variety of outputs we publish to make greater use of our knowledge.

We recognise we can do more to ensure that all our work meets our quality standards, and we draw on the insights from our internal and external quality assurance to help us to continuously improve. This year we have sharpened our focus on making actionable recommendations to help government make sustained improvements against the key areas of risk we have identified in our reports. We published for the first time our recommendations tracker, which provides transparency on how our recommendations have been addressed.

A learning and improvement culture is vital to maintaining the quality of our work in the face of new challenges. In this spirit there are further changes we are introducing in 2022-23 including a new approach to quality assurance, proportionate to the risks and opportunities for impact in each audit. I look forward to reporting on progress in next year's Transparency Report.

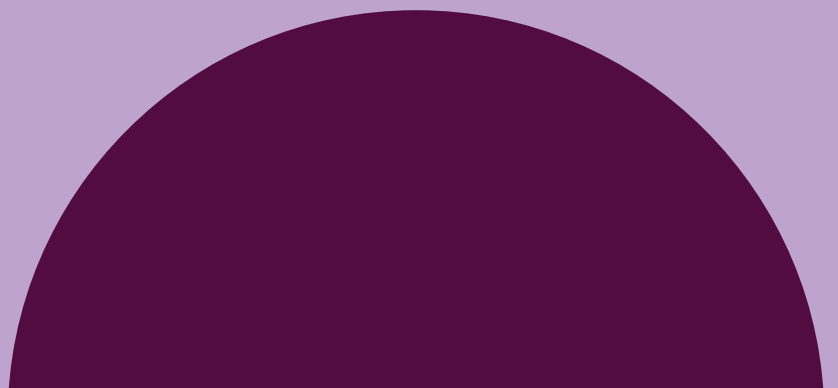
Part One



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Overview

Role of the National Audit Office

1.1 We are the UK's independent public spending watchdog. We scrutinise public spending for Parliament and are independent of government and the civil service. We support Parliament in holding government to account and help to improve public service through our high-quality audits.

1.2 We are required under statute to undertake audits of public sector organisations for Parliament. We audit the financial statements produced by government departments and other public bodies. We also examine and report on the value for money (VfM) of how public money has been spent.

1.3 The National Audit Office (NAO) is led by the Comptroller and Auditor General (C&AG), Gareth Davies, who is an officer of the House of Commons. The C&AG is responsible for making audit judgements, for deciding a programme of VfM examinations and for reporting the results of his work to Parliament. 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. Further information on his role and NAO governance is in Part Four.

Our strategy and values

1.4 We launched a five-year strategy in 2020 (**Figure 1** on page 14).¹ It builds on our established strengths in providing high-quality, effective support to Parliament. It also responds to feedback that we could share our knowledge and insights more effectively to support both accountability and improvement in outcomes and value for money. Increased expectations of the quality and rigour of audit also mean we must modernise how we carry out our audit work.

1.5 We established a set of values (**Figure 2** on page 15) that reflect who we are as an organisation and how we work together and with our stakeholders to achieve our purpose and priorities. We have incorporated these into our organisational life and developed our culture to place greater importance on wellbeing and supporting one another.

¹ The National Audit Office's five-year strategy, 2020 to 2025.
Available at: www.nao.org.uk/wp-content/uploads/2020/05/nao-strategy-2020-25.pdf

Figure 1

Overview of the National Audit Office's (NAO's) strategy 2020-21 to 2024-25

Our purpose

We are the UK's independent public spending watchdog.

We support Parliament in holding government to account and we help improve public services through our high-quality audits.

Our strategic priorities

Improving our support for effective accountability and scrutiny.

We provide assurance that public resources are accounted for accurately and used as intended. When this does not happen, we point it out. We will upgrade our methodology and software to deliver higher-quality audits using data analytics. This will provide Parliament with deeper insights to scrutinise public spending, and those responsible for the governance of the bodies we audit with the assurance they need.

Increasing our impact on outcomes and value for money.

Our work focuses on the issues that matter and we will place greater emphasis on where we can influence long-term value for money. We will make better use of our analytical and audit expertise to identify how public services can be improved. This will allow more insightful and practical recommendations that lead to better outcomes.

Providing more accessible independent insight.

We will be known as a valuable source of knowledge on how well public resources are used and how the governance and performance of public services can be improved. We will synthesise what we know on important issues and make it easier for others to understand and apply the lessons from our work.

Our strategic enablers

We will attract, retain and develop high-quality people.

Our people are proud to be part of our diverse, inclusive and healthy workplace. We attract talented people and support them to become even better at what they do, enhancing their careers and ensuring we have the skills and capabilities we need.

We will make more effective use of technology, data and knowledge.

We use technology and analysis of data to perform our audit work more effectively and to create and communicate new insights that cannot be achieved in other ways.

We aim to be an exemplar organisation.

We lead by example in holding ourselves to the high standards we expect from public bodies. We are efficient, provide value for money and focus on long-term sustainability.

Source: National Audit Office

Figure 2

The National Audit Office's (NAO's) values



Source: National Audit Office

NEXT PAGE:
Our work

Our work

1.6 We help to drive improvements in public spending through the delivery of our financial audits, value-for-money and wider assurance work, as well as through the cross-government perspective we generate looking across all of our work. We use our expertise in these areas to draw out meaningful and impactful insights, including lessons and recommendations for government, helping to drive effective accountability and scrutiny. We support Parliament's scrutiny of government by supporting the work of the Committee of Public Accounts, individual members of Parliament and other select committees with briefings, reports and a programme of secondments.

1.7 The C&AG has a wide range of reporting powers including providing an annual audit opinion on financial statements, assurance work on tax revenue-based accounts, the ability to report on issues of wider interest on accounts, and our VfM remit.

1.8 The C&AG, with the support of the NAO, provides an independent audit opinion on 400 published financial statements, including those of government departments, arm's-length bodies, government-owned companies and other public bodies. This audit work is defined by international auditing standards.

1.9 During 2021-22, the C&AG provided unqualified opinions on most of the 2020-21 financial statements. The C&AG qualified his audit opinion on 14 financial statements highlighting where there were material misstatements or errors within the accounts or where Parliamentary intentions had not been complied with (affecting our 'regularity' opinion).²

1.10 In addition to our financial audit work, we also carry out a range of VfM and wider assurance work to support Parliament in holding government to account. This includes lessons learnt reports and investigations, for example our investigation into the management of personal protection equipment (PPE) contracts in the health sector. During 2021-22, we produced a programme of 58 VfM and wider assurance reports, including 15 on COVID-19 and 18 on other long-term priorities such as major infrastructure projects, the effect of EU Exit, progress towards the net-zero emissions target, the use of technology and data to transform services, and devolution to local government.

² Number as at September 2022. Details of the entities where we qualified the C&AG's opinion are available at: www.nao.org.uk/our-work/financial-audits-overview/

Impact of our work

1.11 We seek to improve outcomes and value for money by making recommendations about the services we examine in our reports. In September 2021, to increase our influence, we launched our [recommendations tracker](#), which brings together NAO recommendations published since April 2019.³ In summary:

- 93% of our recommendations made between 1 April 2019 and 31 March 2021 have been accepted or partially accepted by government; and
- 80% of surveyed senior officials in the bodies we audit agreed that our work leads to better outcomes.

1.12 Each year, we identify cases where our influence has contributed to better public services or financially quantifiable net benefit to the taxpayer. We refer to this as our 'impact'. Our Annual Report and Accounts 2021-22 highlights the financial, wider and long-term impacts brought about through our work.⁴

Feedback from those we audit

1.13 An important measure of the quality and impact of our work is how much it helps public bodies and audit committees to drive improvement in public services. We seek feedback through an annual, independently conducted survey and interview programme and draw on this to support continuous improvement in our audit practices.

Feedback from our clients

1.14 We did not seek feedback from the bodies we audit in 2020 due to the COVID-19 pandemic but results from 2021 continue to highlight financial audit as our core strength. Of the surveyed senior officials in the bodies we audit:

- 91% rated the quality of their most recent financial audit as good (89% in 2019);
- 80% of finance directors and accounting officers agreed that the audit recommendations we made were realistic (77% in 2019); and
- 88% agreed that our teams understood the wider context in which their organisation works and applied it appropriately to the financial audit (90% in 2019).

³ National Audit Office, *NAO Recommendations Tracker*, September 2021. Available at: www.nao.org.uk/nao-recommendations-tracker/

⁴ See pages 46–49 of National Audit Office, *NAO annual report and accounts 2021-22*, June 2022. Available at: www.nao.org.uk/corporate-information/nao-annual-report-and-accounts-2021-22/

1.15 Our VfM work is positively received by the finance directors and accounting officers:

- 78% agreed that our reports are of a good technical quality;
- 76% agreed that the NAO brings a deep and accurate understanding about wider management issues beyond financial management and control matters to its VfM work; and
- 70% agreed that the way the NAO does its VfM work is independent, fair and balanced.

1.16 Some of the learning points we have taken from the feedback are:

- audited bodies tell us that they would welcome greater communication. We have regular channels of communication with senior stakeholders at the bodies we audit, where we discuss our forthcoming work and the impact of our past work. We are introducing further liaison to discuss NAO recommendations and ensure they are actionable; and
- our insights work is very well received by audited bodies and they would welcome us sharing more. We are improving how we use a range of channels to communicate our insights work to audited bodies, including our website, blogs, contact via NAO staff and email alerts.

Feedback from MPs

1.17 MPs are a key audience for our work, supporting Parliamentary scrutiny, and we continue to have a strong reputation in Parliament. In 2021, 72% of MPs said that they have a favourable opinion of the NAO; the highest proportion recorded since we started taking part in the Ipsos Stakeholder Survey of MPs in 2010.

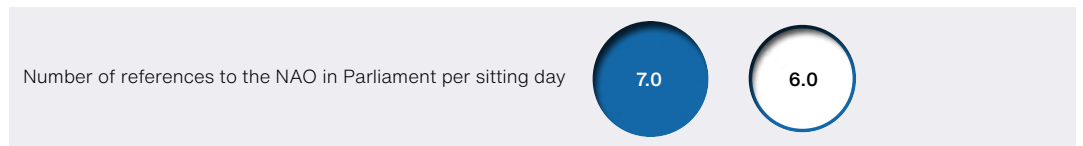
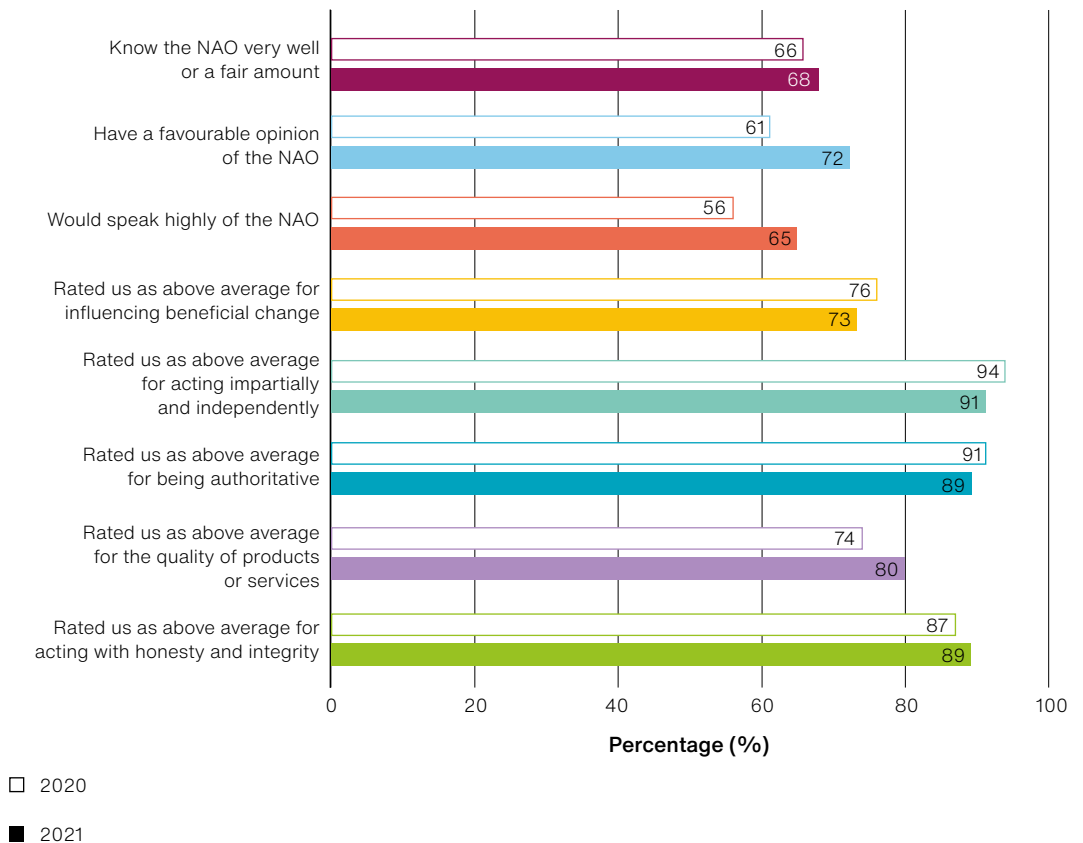
1.18 MPs are increasingly aware of our work and trust us to help them to hold government to account and scrutinise public services, with 90% of MPs agreeing we were effective at this in 2021 (**Figure 3** on page 19). MPs looked to us as a source of information more times in 2021 than in 2020, an average of 14 in comparison to 11.7.

1.19 We have focused on improving our approach to communicating with MPs, after just 41% rated our communication with them as above average in 2019. This has improved, with almost two-thirds saying in winter 2021 that they rate the NAO as above average. MPs tell us that the NAO is communicating more frequently, with the right information, on the right issues and building constructive relationships. Our new redesigned NAO website is also enabling us to respond to the minority of MPs who say that our reports are not easy to find when they need them. Further information on the support we provide to Parliament is available in our Annual Report and Accounts 2021-22.⁵

⁵ See footnote 4, pages 36–39 of NAO annual report and accounts 2021-22, June 2022. Available at: www.nao.org.uk/corporate-information/nao-annual-report-and-accounts-2021-22/

Figure 3

MPs' perception of the National Audit Office (NAO), 2020 and 2021



Notes

- 1 Sample for 2021: 478 MPs contacted, 123 MPs interviewed, 95 MPs answered the National Audit Office questions (versioning used to control interview length).
- 2 Quotas and weighting used so results reflect the House of Commons by political party.
- 3 Broad sample controls also set on region and gender.
- 4 Fieldwork dates for 2021: November 2021 to February 2022. Fieldwork dates for 2020: November to December 2020.

Source: Ipsos MORI MPs Winter 2021 survey; National Audit Office Annual Report and Accounts, 2020-21

Getting back on track

1.20 The COVID-19 pandemic remained a key challenge for our work, both in terms of its impact on the audit risk assessment and on audited bodies' teams and schedules for the production and audit of financial statements.

1.21 The timeliness of reporting is an important part of Parliamentary and public accountability, and was adversely affected by the pandemic. Departments have needed to account for complex and risky expenditure and loan guarantee programmes and there have been unusual demands on the capacity of finance staff. Before the pandemic, we were able to certify 78% of government and arm's-length body accounts before the 2019 summer Parliamentary recess.

1.22 We have adopted a phased approach to getting back to pre-pandemic timetables, prioritising the main government departments. Our goal is by 2024 to complete 80% of our audits by Parliament's summer recess, including all of the main departments.⁶

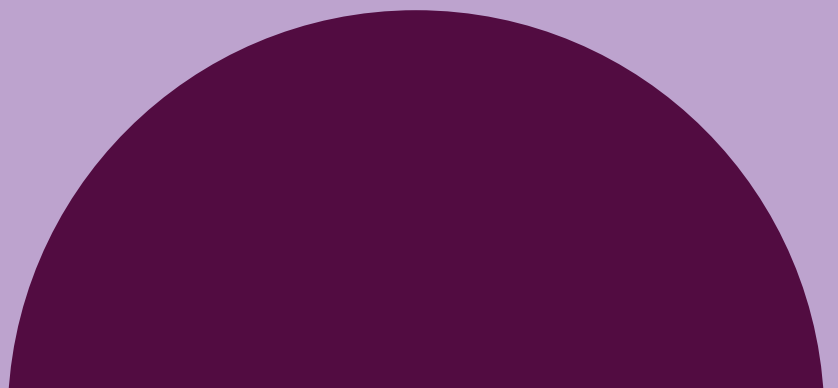
1.23 We completed 59% of the main departmental audits before Parliament's summer recess in 2022 (compared with 47% in 2021 and 39% in 2020). Across all of our audited bodies, we completed 53% of our audits before the recess (55% in 2021 and 41% in 2020). We continue to work with audited bodies to ensure that we are on track to meet our 2024 goal.

⁶ This is defined as the financial statements of the most significant government departments and the BBC Group.

Part Two



TWO
TWO
TWO



Audit independence and quality

How we ensure quality

2.1 The quality of all our work gives us our licence to operate in supporting Parliament in holding government to account. ‘Striving for excellence’ is one of our four values and we want to create a culture where all colleagues share our quality aspirations and challenge any potential barriers to achieving them. Quality is a shared endeavour, and we expect colleagues to consult to draw from expertise across the National Audit Office (NAO), learn from each other and be open to discuss and solve problems when they arise.

2.2 We take a system-wide approach to quality. We provide a framework designed to help colleagues get things right the first time and to make it difficult to get things wrong. We do this by:

- creating an open culture, where people support each other to deliver quality audit work;
- effective people and project management;
- a targeted learning and development programme;
- improving access to appropriate technical support and expertise;
- enhancing independent quality assurance of our audits and ensuring we learn from the feedback; and
- updating audit methodology for our financial audit supported by improved audit software and technology.

2.3 During 2021-22, we have brought increased focus to quality by refreshing a Quality Plan for our financial audit. We are currently revising our quality management arrangements and moving to a more risk-based approach (paragraphs 2.17 and 2.59). Our Audit Quality Board is now in place to challenge the effectiveness of the controls we have in place supporting the quality of all our work (paragraphs 4.18 and 4.19).

Embedding quality

2.4 Our NAO values highlight our ambition for excellence in everything we do and promote a culture of supporting each other to achieve this. We encourage learning and knowledge sharing throughout the organisation and strive continuously to improve our processes and controls. We **learn from our internal and external reviews and use these to inform developments in processes, guidance, support and training**. For example:

- We undertake a programme of ‘root cause analysis’ in our financial audits to help identify the reasons behind quality issues which, in turn, help to inform our Quality Plan and the further actions we should take. We also use this programme to identify good practice and perform reviews over wider thematic issues that impact on particular sectors of our audit portfolio (see case study).
- We hold facilitated lessons-learned sessions with study teams shortly after the publication of their value-for-money (VfM), investigation or wider assurance report. We collate and review insights from these periodically. Through this process, we identify good practice and learning points, which are shared with teams. In cases where we have identified quality issues from these sessions, or through other sources such as cold reviews, we will ask teams to identify the learning for their next piece of work and, where possible, to take immediate steps to rectify the issues. This could include making a correction in published work.

2.5 We have taken significant steps to enhance quality by **strengthening our knowledge management and specialist expertise support** to financial audit, VfM and our wider assurance audit work. Building such expertise enables us to make better use of our accumulated cross-government insights, make more informed judgements and make it easier for those delivering public services to apply the lessons from our work.

2.6 We have continued to:

- develop our **six insight hubs** focused on key cross-cutting issues where we assess there to be opportunities for government to improve its capability. These insight teams cover themes critical for effective delivery in government – analysis, commercial, digital, financial and risk management, major project delivery and people and operations management; and
- embed our **centres of financial audit expertise for pensions, property estimates, financial instruments, and fraud and error** to provide specialist support for audit teams. These are key areas of focus due to their complexity and specialist nature. We also established a new centre to support our charities portfolio of audits this year.

Using root cause analysis to promote audit quality

In addition to performing root cause analysis on individual financial audits, we also worked to understand the wider issues we faced in certain sectors of our portfolio. In 2021, we undertook root cause analysis on quality issues in both the financial instruments and charities sectors of our audits.

- The analysis on financial instruments highlighted the need for enhanced guidance and support for teams. Our Centre of Expertise in Financial Instruments has taken forward the findings from this root cause analysis as it developed its detailed action plan to address recurring quality findings around these audits (see paragraph 2.36 and associated case study).
- The analysis on charities highlighted issues with sector knowledge of specific accounting issues in this area, resourcing and the quality of audit evidence received. These issues are being taken forward by our newly established charities centre of expertise, which has been created to improve the quality and consistency of our charities audits. This will initially focus on the design of audit procedures and supporting teams to deliver high-quality audits.

Our root cause analysis programme will continue to contribute to the evolution of our work through thematic reviews, as well as on specific audits.

2.7 Audit quality also forms a key part of our **performance management framework**. We monitor quality principally through the delivery of annual programmes of internal and external reviews of samples of individual financial and VfM audits. The outcomes from these reviews are considered as part of our performance discussions with relevant directors and their teams. We also have a wider programme of work we currently have under way to develop a comprehensive suite of audit quality indicators to help identify potential risks to the quality of our work as individual audits progress so we can intervene more effectively where needed.

2.8 The rest of this part discusses specific arrangements for our financial audit and VfM workstreams.

Financial audit

2.9 We audit an increasingly complex and challenging portfolio of financial statements. This was amplified even more over the past year due to our need to respond to the exceptional audit risks arising from the UK government's unplanned spending on the COVID-19 pandemic response. As examples of our response, the Comptroller and Auditor General (C&AG) qualified his audit opinions on the 2020-21 financial statements of the Department of Health & Social Care⁷ and the Department for Business, Energy & Industrial Strategy⁸ and reported his findings to Parliament. These reports illustrated the scale and complexity of the audit work required to match the extraordinary nature of the sums spent, written-down or provided for.

2.10 Against this background, we remained committed to ensuring that all our work meets our quality standards and the significant investment we are making continues to have a positive impact on the underlying quality of our financial audit work.

2.11 Some of the measures we have already put in place will take more than one audit cycle to embed and, consequently, will take time to feed into the outcomes from our internal and external inspection programmes. Nevertheless, our 'three lines of defence' assurance model continues to provide us with confidence that our underlying methodologies and NAO-wide approaches are sound (Figure 4 on page 26). We remain on course to deliver our planned improvements. We are also ever vigilant about the challenges facing us given the portfolio we audit and the increasing professional expectations facing the wider audit profession.

2.12 The following section describes our existing quality arrangements. It sets out the challenges we face and our commitment to improving the quality of our financial audits through our Quality Plan.

Quality arrangements: our quality framework

2.13 All our financial audit work must comply with auditing standards. For 2021-22, these include:

- International Standards on Auditing (ISAs) (UK);
- the Financial Reporting Council's Ethical Standard 2019 (the Ethical Standard); and
- International Standard on Quality Control for audits (ISQC 1).

2.14 The C&AG must perform certain discretionary audits under the ISAs (UK). He has chosen to adopt these standards for all statutory UK financial statements audits where a true and fair opinion is required. Meeting these standards means that our financial audit work also complies with the relevant international standards for Supreme Audit Institutions established by the International Organization of Supreme Audit Institutions

⁷ National Audit Office, *Department for Business, Energy & Industrial strategy accounts 2020-21*, November 2021. Available at: www.nao.org.uk/reports/department-for-business-energy-and-industrial-strategy-accounts-2020-21/

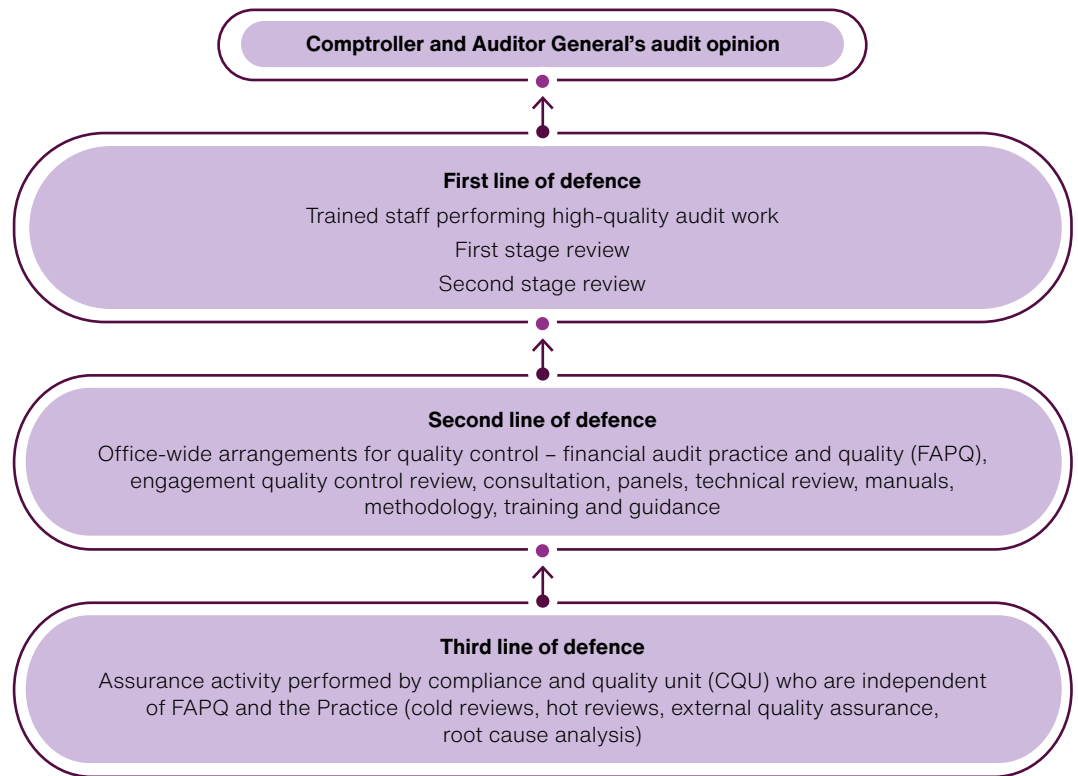
⁸ National Audit Office, *Department of Health & Social Care annual report and accounts 2020-21*, January 2022. Available at: www.nao.org.uk/reports/the-department-of-health-and-social-care-annual-report-and-accounts-2020-2021/

2.15 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.

2.16 We adopt a three lines of defence model to ensure that our audit work complies with the expectations of these standards and best professional practice. **Figure 4** illustrates our current internal quality control framework.

Figure 4

National Audit Office financial audit: the quality control framework



Source: National Audit Office

2.17 We are reviewing these arrangements as we begin to implement the revised International Standard on Quality Management 1 (ISQM) (UK) from December 2022. This includes establishing a detailed quality risk register to support our system of quality management and aligning our quality monitoring processes to the requirements of the new standard.

2.18 Audit teams are responsible for delivering audits that meet auditing standards. They are supported by our Financial Audit Practice and Quality (FAPQ) team, which puts in place wider arrangements to secure the quality of our work including the regular updating of our audit manual and methodology, delivery of professional guidance and training, and providing technical advice and support as requested. Our Compliance and Quality Unit (CQU) undertakes additional assurance activities to assess the quality of audit work and collates findings to help inform future guidance and audit policy.

2.19 We build quality into all stages of a financial audit to ensure that the work is of the highest technical quality. We place a premium on consultation including audit planning consultation meetings, consultations with centres of expertise as well as with our FAPQ team. At the planning stage of an audit, we require those audit teams who audit our higher-risk and more complex financial statements to have an executive director-led audit planning consultation meeting. These meetings provide external challenge to teams and an early opportunity to consult with NAO senior management on key aspects of their audit plans. Other teams can voluntarily hold a director-led session where they consider they would also benefit from consultation and challenge.

2.20 We review our work at a number of specific stages. All work undergoes a two-stage review by senior members of the engagement team. Some audits with significant audit judgements also undergo a quality control review by an independent and experienced director. This additional layer of review is dependent on the nature of the engagement, unusual circumstances or risks, legal and regulatory requirements and the size and complexity of the organisation.

2.21 We also use audit panels to consider and consult on significant audit judgements such as those that might lead to a qualified audit opinion and identify cross-cutting audit issues. These consultation meetings and panels comprise our relevant executive directors, the director of FAPQ, and engagement team.

Support from the Financial Audit Practice and Quality team to the audit team of the Department of Health & Social Care accounts

The audit of the 2020-21 Department of Health & Social Care (DHSC) accounts was one of the most challenging ever undertaken by the NAO. Total operating expenditure increased by £44 billion to £192 billion as DHSC responded to the COVID-19 pandemic in setting up new operations and spending significant amounts of taxpayers' money at pace.

Throughout the audit, the DHSC audit team was supported by the Financial Audit Practice and Quality team (FAPQ), to ensure the audit was planned, undertaken and completed to a high standard. For example:

- **Planning:** The team engaged FAPQ in consultation meetings at the planning stage to shape and develop our approach to auditing the significant risks of material misstatement as we built our understanding of the DHSC's response. There were a large number of new risks resulting from the DHSC's pandemic response. This included audit risks around the mass purchasing of some £12 billion of personal protective equipment and the establishment of the NHS Test and Trace programme.
- **Audit judgements:** The DHSC audit team worked closely with FAPQ over complex accounting and audit judgements. This included close technical consultation around the audit response to the limitations in evidence available to us in respect of: inventory and accruals; the regularity qualifications of the DHSC's COVID-19 fraud assessment; and DHSC's non-compliance with HM Treasury requirements for £1.3 billion of spend.
- **Supporting Parliamentary scrutiny:** FAPQ supported the audit team as they prepared for a Committee of Public Accounts session in March 2022 on the DHSC Annual Report and Accounts 2020-21.

The C&AG's qualification of his audit opinion and his associated report on the accounts emphasised the need for DHSC to be accountable to drive improvements in controls around inventory, accruals, regularity of expenditure, and related parties.⁹

Publication of the DHSC 2020-21 Accounts on 31 January 2022 generated significant press and public interest, with many news outlets covering the NAO's findings.

⁹ See footnote 8.

2.22 CQU reviews a sample of audits in progress ('hot reviews').

These reviews focus on our higher-risk and more complex audits. They are undertaken by independent and experienced audit managers at the planning stage and before the audit opinion is signed to provide further assurance to the C&AG over the quality of the work performed by audit teams.

Quality assurance arrangements: internal and external monitoring

2.23 The quality of our financial audit work is our key priority and features within our corporate risk register. We measure the quality of our work through an annual programme of internal and external inspections of a sample of individual audits. Our target is that, should an audit be inspected by an independent reviewer, they would be judged to be good or requiring only limited improvement.

Internal inspection programme

2.24 CQU coordinates an annual internal quality assurance programme by reviewing a sample of completed audits each year. These reviews are undertaken by experienced audit managers, overseen by financial audit directors. The purpose of each review is to make sure that we have complied with our *Financial Audit Manual* and International Standards on Auditing.

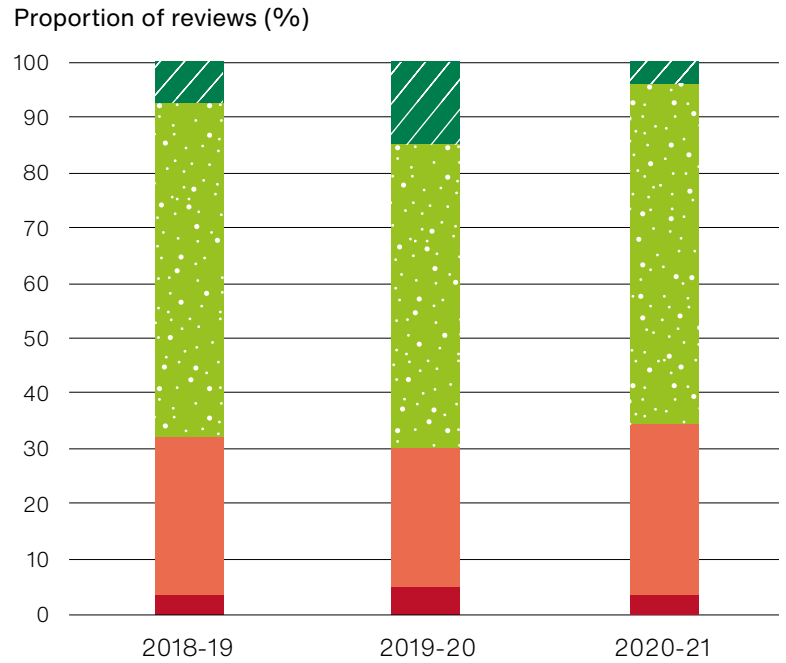
2.25 During 2021-22, we reviewed 26 of our 2020-21 audits (20 of our 2019-20 audits in 2020-21). Of these, some 65% (70% in 2020-21) were judged to be good or required only limited improvements. **Figure 5** on page 30 shows the results from our internal quality reviews over the last three years.

External inspection programme

2.26 The Audit Quality Review team of the Financial Reporting Council (FRC) reviewed a sample of nine 2020-21 audits (five audited under the Companies Act and four from the rest of our portfolio of audits), compared to seven in 2019-20. Of these, some 56% (71% in 2020-21) were judged to be good or requiring only limited improvements though 44% (29%) in 2020-21 required improvement. None of our audits required significant improvements. **Figure 6** on page 31 shows the results from our external quality reviews over the past three years.

Figure 5

National Audit Office (NAO) results from internal quality reviews from 2018-19 to 2020-21

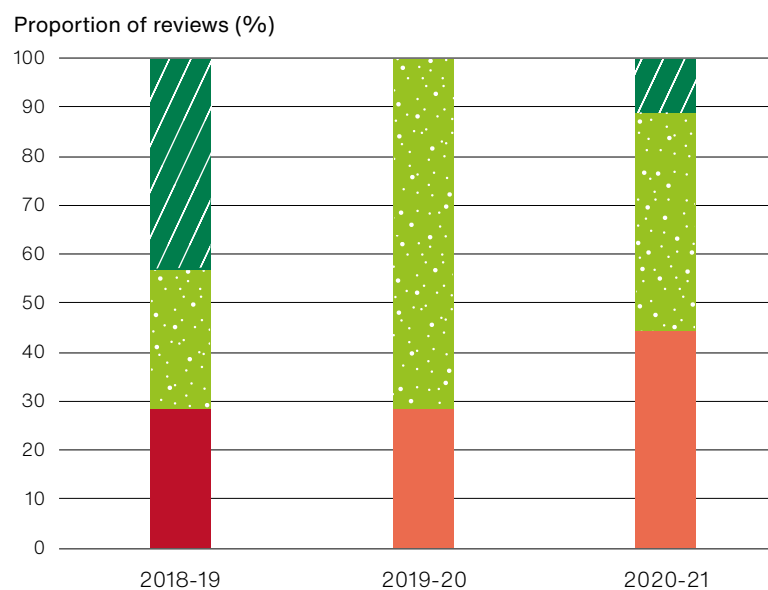


Above the quality threshold			
Green - good	2	3	1
Amber/green - limited improvements required	17	11	16
Below the quality threshold			
Amber/red - improvements required	8	5	8
Red - significant improvements required	1	1	1
Total	28	20	26

Source: National Audit Office results from internal quality reviews

Figure 6

National Audit Office (NAO) results from external quality reviews from 2018-19 to 2020-21



Above the quality threshold			
Green - good	3	-	1
Amber/green - limited improvements required	2	5	4
Below the quality threshold			
Amber/red - improvements required	-	2	4
Red - significant improvements required	2	-	-
Total	7	7	9

Source: National Audit Office results from external quality reviews

Issues raised from these inspection programmes

2.27 Our review programmes highlight that we need to do more to:

- improve our **challenge in areas of judgement**, in particular for key assumptions used in valuations and estimates and the use of experts, and ensure that this challenge is thoroughly documented;
- increase the extent of our work on the **valuation of harder to value assets and investments**, especially those relating to pension assets;
- ensure consistency in the quality of **more complex financial services audits**;
- strengthen the **group auditor’s oversight of key component auditors** where we are auditing group financial statements;

- ensure we fully **document our approach to testing journals** and how it addresses the potential risk of fraud or management manipulation; and
- improve the **evidence of our oversight and direction** of those audits we contract out to our framework partners.

2.28 Although these issues are consistent with those raised with private sector audit firms, the findings also show that we have more to do to consistently achieve high-quality work and to keep pace with the rising quality bar for the audit profession. The steps we are taking to achieve this are set out in our Financial Audit Quality Plan (see paragraph 2.33). We are confident that the ambitious programme of change set out in our Plan is focused on the right areas and is supporting teams to deliver high-quality audit work on a more consistent and systematic basis. We know that some of the improvements we have in progress will take a number of audit cycles before they are fully embedded. However, our plans for improvement remain on track and will provide a sound platform to address the issues highlighted by our inspection programmes.

2.29 More details of the findings from these reviews, and the progress we have already made following last year's external inspection programme, are at Appendix Two.

Learning from individual reviews

2.30 When an individual audit is reviewed internally or externally, the audit team agree with the reviewers the areas for improvement they need to take forward in the subsequent audit. Depending on the significance of the findings within each review, we consider additional support for teams as they take forward their agreed actions. For example, we may undertake a root cause analysis session (paragraph 2.4) to get to the heart of why an audit needed improvement, which may lead to further actions. We also may include an audit within our programme of hot reviews (paragraph 2.22) to ensure actions have been taken forward subsequently.

2.31 Within this context, individual audit teams consider the impact of these findings on their subsequent audit. For example, this may include reconsidering the risks of material misstatement, re-assessing the sufficiency of evidence needed to support their previous audit judgements, the skills and expertise needed to undertake this audit, and discussions with the audited bodies as to the additional evidence needed.

2.32 We consider findings from these individual reviews, as well as those from our root cause analysis programme, to drive further improvements in our methodologies and guidance for application across our wider portfolio of audits.

Financial Audit Quality Plan

2.33 In January 2021, we published our first Financial Audit Quality Plan. This set out the improvements and steps we are taking over 2020-21 to 2024-25 to improve the quality of our work and to support teams to achieve our quality ambitions. We have adopted a whole-system approach to audit quality. This means that individual colleagues and teams operate in a culture and set of systems that are designed to ensure that quality standards are consistently met. The breadth of the Plan reflects this and covers our values, learning and development, formal training, sharing of good practice, technical support, review and governance.

2.34 In December 2021, we published our second Quality Plan, which builds on the first plan and highlights the progress we are making to address findings from our inspection programmes, together with the interventions we have in place to support our 2021-22 cycle of financial audits. Our Plan points to the significant investment we are making in our use of technology and, in particular, our Audit Transformation Programme.

2.35 This programme will introduce revised methodologies driven by the introduction of new auditing standards and new software to improve the quality and efficiency of our financial audits through higher levels of standardisation and automation (paragraphs 2.41 to 2.43). It represents a once in a generation investment for the NAO and will see a real step-change in the quality of our audit work. It is being implemented from the 2022-23 audit cycle. In the meantime, our Quality Plan highlights the additional measures we are taking to support teams to deliver high-quality audit work. **Figure 7** on pages 34 and 35 sets out our progress against the Quality Plan and future priorities.

2.36 An important area of focus for us during 2021-22 was to respond to the Financial Reporting Council's (FRC's) observation on the quality of our work on our financial service audits and more complex financial services-related balances on other audits. A key response has been the development of our Centre of Expertise in Financial Instruments. We established this in 2020 to provide expert support to audit teams and to continue to develop our new methodology and invest in training in areas of complex estimates and valuation. During 2021-22, the centre produced additional guidance to teams on auditing harder to value transactions and also developed a detailed action plan to better identify where its support should be targeted within the NAO, the further investment it needs to make, and the additional expertise it requires, including from our framework partners. The case study highlights the work done so far and our further ambitions.

Figure 7
Financial Audit Quality Plan actions

Area	Progress during 2021-22	Key priorities going forward
An open culture	<ul style="list-style-type: none"> Shared lessons learnt from our reviews in a more transparent way and as inspection programmes get under way. Discussed these lessons with grade groups, including director masterclasses to help explore quality issues. Embedded the role of the financial audit service line directors in each group to help promote audit quality. 	<ul style="list-style-type: none"> Embed our cultural change and the importance of our values. Continue to learn from our experiences of auditing through a mixture of remote and office-based working.
People management	<ul style="list-style-type: none"> More focus on people management and reflection on the performance coach role that was introduced last year. Continued to increase our financial audit staff to enable us to deliver a greater number of our audits to a pre-summer recess timetable and address the increasing audit quality bar. 	<ul style="list-style-type: none"> We will take stock of the role and effectiveness of our performance coaches, including refreshing and rebalancing coaches to keep pace with people's moves and capacity. We will continue to highlight the importance of recognising good-quality work in people's appraisals.
Learning and development	<p>Colleagues can access a wide variety of learning and development through an audit skills portal. During 2021-22, we introduced new mandatory training and support packages on thematic issues arising from previous quality reviews, such as on testing journals, sufficiency of audit evidence, and auditing estimates.</p>	<ul style="list-style-type: none"> We are developing an extensive learning and development package which will support our Audit Transformation Programme and its implementation. We will take into account recommendations arising from the 2020-21 internal and external inspection programmes.
Second line of defence	<ul style="list-style-type: none"> We have new framework partners who worked with us from our 2021-22 audits. Updated our methodology in response to the Financial Reporting Council's (FRC's) findings on our 2019-20 audits. For example, we developed a revised sampling approach and methodology. Provided new and more focused training for our directors undertaking Engagement Quality Control Reviews (EQCR) Enhanced our existing centres of expertise which support audit teams in the specialist and complex areas of pensions and property. Investing more in our Centre of Expertise in Financial Instruments so that audit teams can seek support in this complex area through our own in-house expertise informed by external expertise where there is a need (see paragraph 2.36). 	<p>The new quality standards, ISQM1 & 2, come into effect from December 2022 (applicable from our 2022-23 audits). We are currently reviewing our existing NAO-wide procedures (which cover all our audit work, including value for money) to identify how these need to be reformed or enhanced to ensure we comply with these standards.</p> <p>We have established a new charities centre of expertise to improve the quality and consistency of our charities audits.</p>

Figure 7 continued
Financial Audit Quality Plan actions

Area	Progress during 2021-22	Key priorities going forward
Third line of defence	<ul style="list-style-type: none"> ● We expanded our cold review and root cause analysis programmes to focus on more thematic issues as well as issues on specific audits. ● Horizon scanning to learn from Audit Quality Review and FRC. ● Shared emerging findings from our hot reviews and our internal and external inspection programmes as soon as they were available so that teams could address issues as quickly as possible. 	<ul style="list-style-type: none"> ● Continue with horizon scanning to help identify areas of focus and changes that need to be made. ● Adopt changes to our NAO-wide review and root cause analysis to meet the new quality standards and bring these programmes forward where we can.
Managing our programmes of work	<ul style="list-style-type: none"> ● Worked to complete more of our 2021-22 departmental audits before the summer Parliamentary recess 2022 compared with 2021 – but not at the expense of audit quality. ● Focused on setting fees that better reflect quality requirements and will enable us to budget and plan more effectively. 	<p>We will develop audit quality indicators so we can take early action to mitigate any potential risk to quality while audits are in progress.</p>
Audit Transformation (see also paragraphs 2.41 to 2.43)	<ul style="list-style-type: none"> ● Piloted our new approach with a small number of teams on lower-risk audits for the 2021-22 audit cycle. ● Engaging with the wider financial audit community to provide progress on developments. ● Procured a strategic partner for our new audit software. 	<p>We are launching our new planning tools in line with the revised ISA 315 risk assessment auditing standard across all our 2022-23 audit work. To support this, in autumn 2022, we will start running modular training to cover all stages of our audit methodology with a focus on sampling, planning and risk assessment.</p>

Source: National Audit Office

Developing our expertise in auditing financial instruments

We have responded to feedback from the Audit Quality Review (AQR) team on the audit of financial instruments by further developing our financial instruments centre of expertise. The centre supported financial audit in 2021-22 by:

- providing technical advice and recommendations in relation to financial instrument-related accountancy queries and audit methodology questions;
- issuing sources of guidance and advice, including an office-wide guide to financial instruments;
- producing a landscape review of financial instruments held by audited entities across central government, to better target support and quality interventions;
- building relationships with external experts and specialists to provide audit teams with targeted and bespoke support on the most challenging queries;
- running root cause analysis sessions in partnership with our Compliance and Quality Unit to better understand why our work on financial instruments is not consistently meeting AQR expectations; and
- contributing to the financial instruments sections of the Audit Transformation Programme.

In 2022-23, we are expanding the resources and remit of the centre to pilot an advisory delivery operating model. This will involve trialling the delivery of specific financial instrument audit workstreams on selected audits directly by specialists. We aim to produce more guidance material, to develop training as well as continuing to offer a consultation service to the rest of the service line.

Source: National Audit Office

2.37 In December 2021, the FRC announced the areas of focus for its audit quality reviews for 2022-23. Therefore, in addition to those highlighted in paragraph 2.27, we are taking further action to support our teams on:

- **estimates including provisions, contingent liabilities and impairment of assets:** During 2021, we introduced our estimates toolkit, which has helped audit teams to better assess risk and develop their audit approach to estimates at the planning stage. We launched a mandatory training module on ISA 540 *Auditing Accounting Estimates and Related Disclosures* in 2021;
- **group audits:** we will consider the implications of the new auditing standard on auditing group accounts, alongside findings from our recent external inspection programme, for our audit work;

- **addressing the risk of fraud:** We have embedded our fraud and error centre of expertise to support the quality of our work around fraud and error. In March 2021, we published a guide to help reduce the risk of fraud and error; and
- **climate risk:** this follows the FRC's review of climate reporting, which identified the need for auditors to improve their consideration of climate-related risks when planning and executing their audits. We launched mandatory training on climate change to help audit teams identify potential risks to their audited bodies. In August 2021, we also published a related good practice guide for audit committees.¹⁰

Investment in technology

2.38 Technology and data analysis help us perform our audit work more effectively and create new ways in which we can communicate our insights. They play an important role in both our financial audit and VfM work, as well as helping us run our own organisation more efficiently.

2.39 In order to support the greater consistency in the quality of our audit work, we have embedded reliable technology tools and associated systems. For example, our use of online toolkits and associated systems has been essential in promoting more collaborative working and consistent outcomes.

2.40 Our technology includes systems used to document our audit work, share data securely with the bodies we audit and analyse financial data. Another key part of our technology infrastructure has been video conferencing systems, ensuring we can communicate effectively with our audited bodies even during periods when our teams were unable to travel to client sites due to the COVID-19 pandemic. All our key systems are cloud-based, which facilitates remote support. Our increased reliance on technology tools for all aspects of our work means we continue to invest in our cyber-security protection measures.

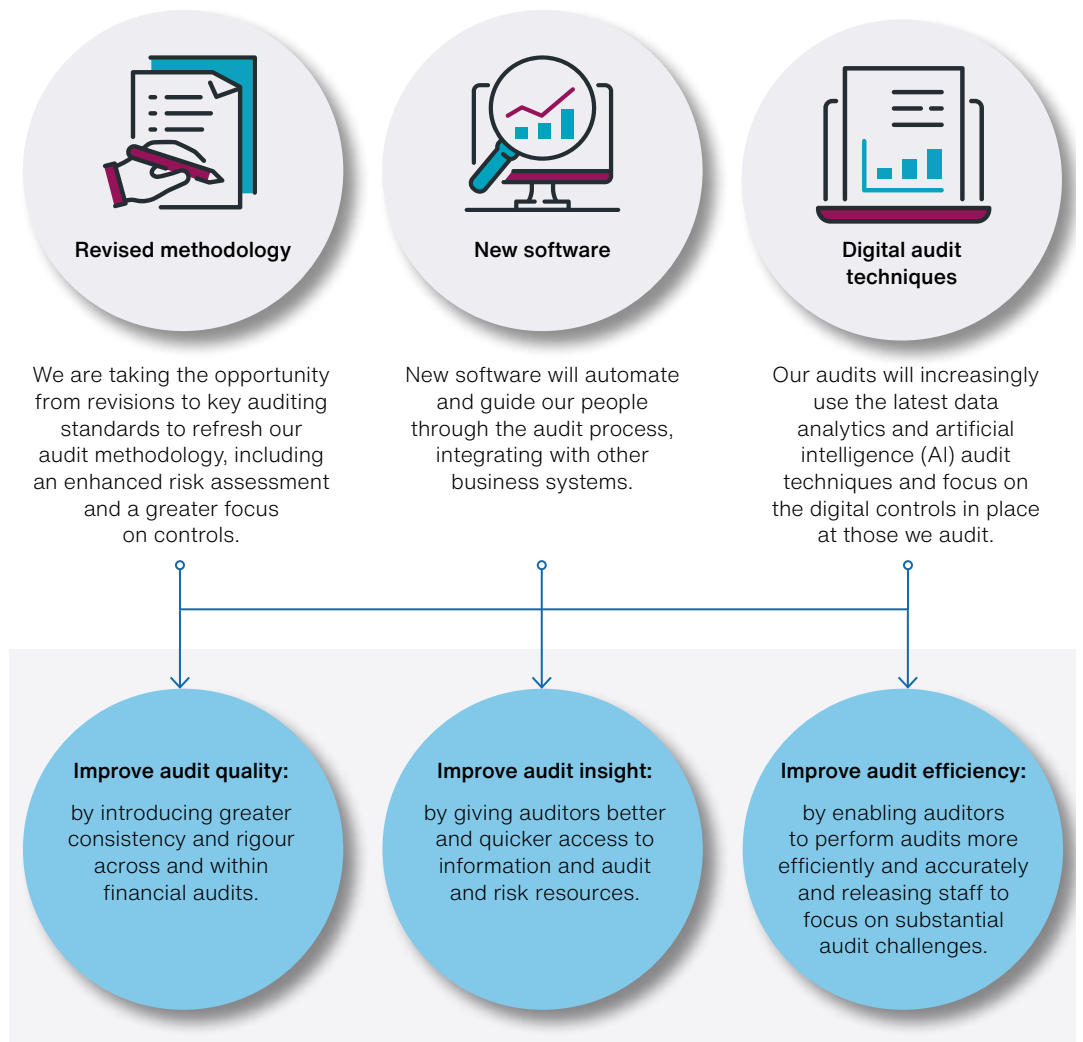
Audit Transformation Programme

2.41 A key investment is the delivery of our Audit Transformation Programme (ATP). ATP is our programme to deliver modern financial audits (**Figure 8** on page 38) of a consistently high audit quality. It will ensure our audits continue to support effective accountability and quality financial reporting and financial management. We are taking an incremental approach, carrying out a phased delivery over several years. We will also make increasing use of data analytics to help assess and inform our response to audit risk.

¹⁰ National Audit Office, *Climate change risk: a good practice guide for Audit and Risk Assurance Committees*, August 2021. Available at: www.nao.org.uk/insights/climate-change-risk-a-good-practice-guide-for-audit-and-risk-assurance-committees/

Figure 8
Our Audit Transformation Programme

We are making a once in a generation investment in our audit methodology and the technology we will use to deliver this. We are taking an incremental approach which over the coming years will transform our audit service, improving quality, insight and efficiency



Source: National Audit Office

2.42 During 2021-22, we refreshed our audit methodology to become more risk-focused, data-driven and analytically sophisticated, including new planning and evaluation tools, and are piloting a new risk assessment tool on six of our 2021-22 smaller audits (see case study).

Case study

The Disclosure and Barring Service audit team's experience of piloting our new audit methodology

As one of the 2021-22 pilot audits for the Audit Transformation Programme (ATP), we have become familiar with the new ISA 315 auditing standard on audit risk assessment and have had an opportunity to influence the tools and templates that will be used by the wider office from 2022-23.

The team received tailored training prior to the pilot audit, which allowed us to understand what is changing and why. The central ATP team have been available throughout the pilot audit to answer questions and provide support. There have been issues with the software, but these were always dealt with efficiently, enabling our team to adapt to and overcome challenges.

Throughout the pilot audit, we were able to suggest improvements to the design and functionality of tools and templates. After using the Risk Assessment Planning Tool (RAPT) and new planning templates, we provided feedback on the time taken to complete the RAPT and suggested the number of questions be reduced. We also suggested ways that some templates could be clarified so they are easier to understand. Our feedback also helped shape the guidance and training being developed for roll-out.

We have benefitted from our involvement on the pilot and are in an advantageous position ahead of transformation to the new audit methodology in 2022-23. We will be able to assist our colleagues next year using our understanding of the tools, methodology and challenges we have faced this year. It has been rewarding to have an impact on the future audit methodology in the NAO.

2.43 We have also appointed a strategic partner to help us further develop new audit software incorporating workflow, automation and analytics. In 2022-23, we will be further piloting the new methodology and expect full implementation in 2023-24.

Wider assurance

2.44 As in previous years, we have again delivered high-quality VfM and wider assurance work that largely meets our standards. We have achieved this in a year where we have produced timely and impactful reports at pace on COVID-19 and other high-profile topics and also expanded the variety of outputs we publish. There is more we can and are doing to ensure all work meets our quality standards and fully embed a learning culture. The valuable insights from our internal and external quality assurance highlight opportunities for us to continuously improve.

2.45 This section describes our existing quality arrangements for VfM and wider assurance work; the findings from internal and external reviews of this work; and the changes we will be introducing for 2022-23.

Quality arrangements: VfM standards and quality approach

2.46 All of our VfM and other wider assurance work must meet a core set of principles set out in our VfM audit standards. These standards are consistent with the Fundamental Auditing Principles of the International Standards of Supreme Audit Institutions, tailored to meet the specific expectations and requirements of Parliament and the UK public sector. We provide teams with detailed guidance to help them meet the standards.

2.47 Producing high-quality VfM and wider assurance work, in line with our standards, is critical to achieving our strategic objectives (paragraph 1.4). Our quality approach is designed to address the two main areas of risk to the quality of our work:

- **Strategic quality** – we should be reporting on, and following up, issues of strategic relevance to Parliament and our audited bodies on a timely basis; otherwise we risk not having the impact we want from our work. Examples of our approach to achieving strategic quality include:
 - **how we select our work** – twice a year, the C&AG will determine our future programme of work to ensure that it focuses on the most significant value-for-money risks to government, both immediate and in the longer term. He will consider suggestions from Parliament, along with our internal assessments of value-for-money risks to government; and
 - **how we get impact from our recommendations** – we expect that the recommendations we make should be clear, focused on the actions government needs to make and likely to lead to sustained, significant improvements against the key areas of risk we have identified in our reports. Our teams follow up progress with departments after publication of our reports. We published this year for the first time our recommendations tracker, which provides transparency on how our recommendations have been addressed.¹¹

¹¹ National Audit Office, *NAO Recommendations Tracker*, September 2021. Available at: www.nao.org.uk/nao-recommendations-tracker/

- **Technical quality** – our work should be accurate, underpinned by a robust evidence base and meet our standards. Examples of our quality approach include:
 - a requirement for peer review at all stages of the work. Depending on the type of work this may come from an experienced VfM practitioner independent of the study team, who will act as a constructive critic to the work. In other cases, peer review can also come from VfM colleagues with specific expertise in a relevant field;
 - a quality assurance review of innovative or complex methodologies by specialists from our analysis hub to check that the results are accurate and that the methodology used is robust; and
 - linking of all statements and data in our work to source evidence in our audit files.

2.48 Our quality approach is formed of a set of activities to ensure that, once selected, all our VfM and wider assurance work remain strategically well positioned, clearly presented and well evidenced.

- **Study team:** Directors and their study teams are responsible for developing and implementing a quality assurance plan, which is agreed by the executive director and an independent director within their group (business unit). This will include delivering the work to the standard expected and conducting review within the team.
- **Review outside of the team:** This will include peer review from a partner director who acts as a constructive critic and a case manager to provide technical and practical advice and guidance throughout the audit. We also ask teams to assess other risks to quality and impact, and to put in place plans to mitigate those risks. For example, teams carrying out complex judgements or analysis may ask specialists in the NAO to review their work. There will also be technical reviews of our graphics and written content.
- **C&AG:** The C&AG will approve the work at specific stages, including scope, emerging findings and the final report.
- **Support:** Study teams are supported by the work of our Value-for-Money Practice and Quality team, which puts in place wider arrangements to secure and monitor the quality of our work including maintaining guidance on our quality approach, the delivery of the annual assurance update training, and providing technical advice and support as requested.

Further details on our quality approach are set out in Appendix One.

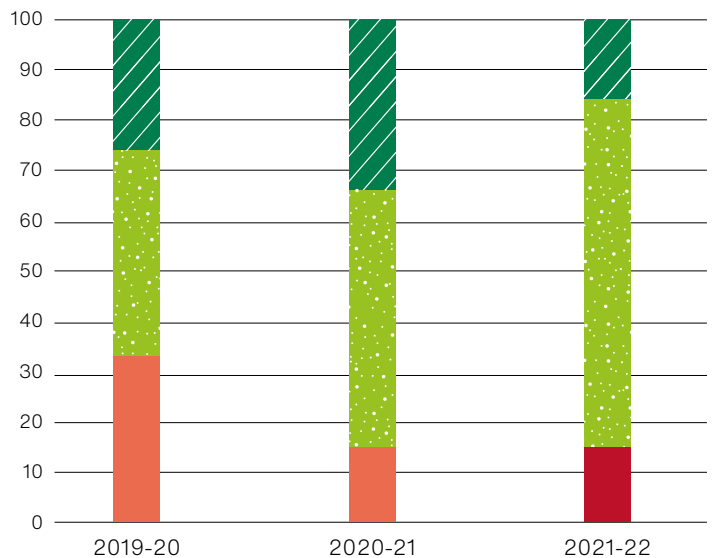
Quality assurance arrangements: internal and external monitoring

2.49 We carry out an internal review of a sample of our wider assurance work twice a year. These reviews check whether our work met our VfM standards and whether quality assurance requirements were followed, as well as identifying good practices. We use the findings to help improve our processes and guidance to staff, supported by additional training where needed.

2.50 In 2021-22, we reviewed 12 VfM studies, investigations and knowledge products. The same proportion of 2021-22 reviews met our standards as last year (10 of 12). This was an improvement on 2019-20, when eight of 12 reports met our standards. However, in this year’s round, two reports received the lowest rating of significant areas for improvement (Figure 9), a rating that the review panel had not given in the previous two years.

Figure 9

National Audit Office (NAO) internal value-for-money cold review results between 2019-20 and 2021-22



Above the quality threshold				
	Green – good/best practice	3	4	2
	Amber/green – good with limited improvements needed	5	6	8
Below the quality threshold				
	Amber/red – areas for improvement	4	2	0
	Red – significant areas for improvement	0	0	2
Total		12	12	12

Source: National Audit Office results from internal quality reviews

2.51 Our 2021-22 reviews found good practices in how teams set out clear evidence trails and documented review, including working collaboratively with financial audit colleagues or specialists in our insight teams to make best use of our knowledge. There were also good examples of teams finding ways to get impact by working with clients or discussing their work through blogs or at conferences. Compared with previous years, we also saw improvements in compliance with ethical declarations and audit closedown following the introduction of our new audit file software.

2.52 In the two cases that did not meet standards, there were weaknesses in the audit file on the documentation of evidence and senior review and we have asked the teams to address these documentation weaknesses. We did not identify any impact on the C&AG's judgements or conclusions from our reviews of these two reports. Among the other 10 reviews, there were more minor examples of areas for improvement. For instance, some methodology appendices could have been clearer about the work we had done and how this supported our judgements.

2.53 Each year, we invite external specialists to review a separate sample of published VfM reports and investigations. In 2021-22, RAND Europe and Risk Solutions reviewed 14 reports between them. This was two more than in previous years to reflect a wider range of our publications. The reviews considered the scope, purpose and context of the report; key messages; how far the report met its purpose; the synthesis of analysis; recommendations; structure and presentation; relevance of content; quantitative and qualitative analysis; graphics; and methods, leading to an overall assessment. This is the third year that we have asked RAND Europe and Risk Solutions to summarise their findings across the reports they have reviewed and more details can be found in Appendix Two. **Figure 10** on page 44 shows external cold review results between 2019-20 and 2021-22.

2.54 The reviewers assessed all the reviewed reports as meeting or exceeding expected standards, as they did in the previous year, with each report having scored a 3 or higher out of the possible 5 rating.

2.55 Overall, reviewers' feedback suggested that strengths included well described scope, purpose and context in most cases. The reviewers also commented favourably on the coherent structure and presentation of reports. Summaries were generally well written and provided a fair and balanced reflection of the contents of the report. Reviewers commented that graphics were often used well to support and complement the text.

2.56 The reviewers also highlighted the following areas with scope for improvement:

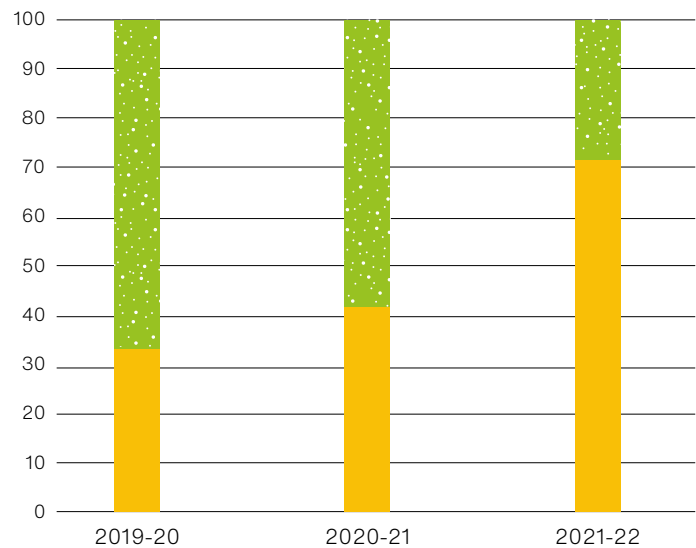
- Reports, and summaries in particular, could have been more concise although, in some cases, it would also have been helpful to have made clearer the purpose of the work, including timing and intended audience.
- There were opportunities for explicit or stronger judgements in some reports' conclusions. Reviewers also believed that some reports would benefit from more extensive analysis to better support their scope and purpose.
- The clarity and targeting of recommendations needed greater specificity in some cases.






- Methodologies continued to require more detail, particularly on how qualitative data were collected and used. However, there were some examples of improved practice in methodology descriptions.

2.57 The areas for learning and improvement identified in 2021-22 across both internal and external cold reviews will underpin our 2022 annual assurance update, consisting of mandatory continuous professional development modules to be delivered in June and September. The cold review findings have also influenced our priorities for organisational development and the focus of our learning and development programme for the year ahead.

Figure 10

National Audit Office (NAO) external value-for-money cold review results between 2019-20 and 2021-22



Above the quality threshold			
 Exemplary – good-practice example	0	0	0
 Amber/green – above average/strong performance	8	7	4
 Amber – sound performance and the expected standard for an organisation such as the NAO	4	5	10
Below the quality threshold			
 Amber/red – below average performance	0	0	0
 Red – very poor performance – inherent risk to the NAO	0	0	0
Total	12	12	14

Source: National Audit Office results from external quality reviews

VfM and wider assurance quality plans

2.58 We have continued to make progress with the commitments set out in our Organisational Development Plan to improve the quality and efficiency of our approach to producing VfM and wider assurance work. This has built upon the completion of our *Modernising VfM* project last year, which introduced new software, tools and streamlined processes to improve the efficiency of how we produce our reports.

2.59 A key change in 2022-23 will be the introduction of a revised approach to quality management. Previously our approach to quality has favoured compliance with a set of quality activities that our teams should meet. Some of the learning points from internal feedback suggested that more tailored quality activities would be valuable. For example, expecting teams to commission focused review from experts under our new approach, rather than asking teams to follow standard review procedures in all cases, should result in more informed, better targeted synthesis and recommendations. Our new approach to quality management will also be more flexible and risk-based to reflect the wider range of report types we publish and the different risk profiles each piece of work will have. For example, some reports may have to be produced rapidly to have timely impact – requiring a greater focus on the most critical quality activities.

2.60 Under the revised approach, teams will have greater responsibility for agreeing the nature and timing of the quality activities that they build into their work, and for responding to changes in the risk profile. As a result, there will be greater ownership for quality throughout all of our teams and grades, and greater understanding of how we manage the risks we face as an organisation.

2.61 We will continue to specify some minimum, mandatory requirements, for example to ensure that we meet legal and ethical requirements and to meet our standards. We have developed a framework of risks that affect every piece of work that we produce to ensure that these are mitigated as we encourage greater flexibility and freedom in other areas.

2.62 To support teams with the new approach, we introduced new guidance in summer 2022. This includes activities, tools and resources to help our teams to manage risks and provide examples of good practice. Examples of how our guidance is changing in response to feedback on how we can improve are set out in the case study.

2.63 We have also incorporated the feedback we have received in our priorities for 2022-23. For example, we are refreshing our guidance about writing style for external publications. We will offer learning and development opportunities to our people related to this, which we intend to improve the clarity of our reports. More detail about how we develop skills among wider assurance staff is in Part Three.

Guarding against strategic risks through our new guidance on risk-based quality management

Revisions to how we form and agree our recommendations

Recommendations in our reports are one of the main ways we can maximise the impact from our work and influence positive improvements to public services. The revised processes for agreeing and following up recommendations will help teams produce recommendations that are realistic and supported by clients. They will also provide better clarity on how teams can work with clients to implement them. New processes will include:

- earlier discussions with audited bodies including a new requirement to hold a session focused on recommendations during clearance, when we agree our report with the audited body before publication; and
- implementation plans to follow up with audited bodies and support their progress with implementing recommendations.

Revisions to how we describe our methods and approach in our reports

It is important that we are able to demonstrate to our readers that the evidence base on which our conclusions are based is robust and credible. Our revised guidance aims to help teams demonstrate more consistently the steps and methods we took to reach our conclusions and any limitations to our work, which guards against readers (or us) misrepresenting what we have examined and reported on. Revisions include:

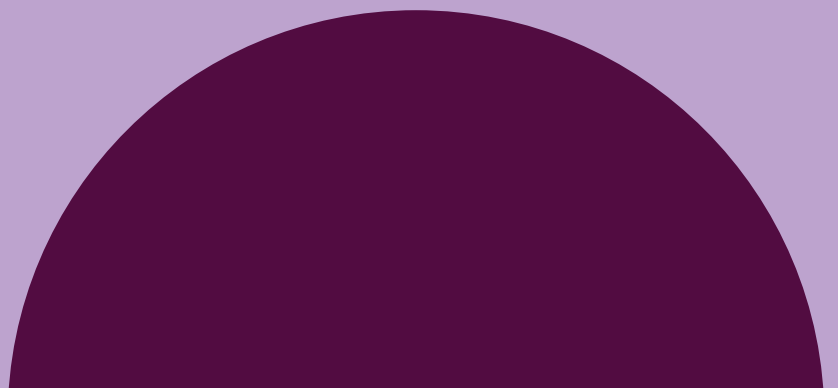
- new guidance on writing a methodology appendix, including what principles to follow and examples of write-ups by method; and
- a new requirement for all teams to include in the summary certain details about the scope and nature of the work we have carried out, such as government's objectives or policy goals and, for evaluative reports, the evaluative criteria or what good value for money would look like.

Revisions to our data presentation standards

Graphics are an important part of our published work and, when used correctly, add value and insight. The revised guidance aims to make it easier for teams to comply with the standards and quality assurance arrangements needed to ensure our graphics are consistently high quality. This includes:

- greater clarity to our teams over the standards that must apply to all of our graphics; and
- easy guides for graphics we commonly use.

Part Three



People

3.1 In line with our strategic priority to take forward our commitment to people development, we have focused more on personal and career development, invested in improving line management and ensuring we have the right skills, removed barriers to diversity and inclusion and supported staff through the pandemic to achieve a good work-life balance.

3.2 This part highlights the actions we are taking to manage ethics, develop our people and the investment we are making in enhancing their skills.

Safeguarding our independence

3.3 For our work to have the impact and influence required, and for Parliament and the wider public to have confidence in the quality of our work, we must uphold high standards of ethics and integrity and work within a framework of values that preserve audit independence.

3.4 The National Audit Office (NAO) is compliant with the Financial Reporting Council's Revised Ethical Standard, which applies to both financial and non-financial audit work. The Ethical Standard 2019 sets out overarching principles of integrity, objectivity and independence. It includes specific circumstances that might arise in audit and other public interest assurance engagements which could undermine this basis for user trust and confidence. We are required to establish that we have identified and addressed relevant conditions and circumstances.

3.5 The Comptroller and Auditor General (C&AG) is the designated ethics partner and has overall responsibility for ethical matters. His independence is enshrined in statute as is our appointment as the external auditor of most of the entities we audit (including value-for-money (VfM) audits). This means that the audited entity cannot replace us as an auditor in response to negative audit opinions or conclusions. Moreover, we are not dependent on fees for non-audit services to audited entities. This reduces threats to independence that could arise from an auditor seeking to protect non-audit income. However, to prevent over-familiarity with the audited entity, we regularly rotate staff in line with the requirements of professional standards.

3.6 We are alert to areas where the NAO or our engagement teams' independence and objectivity could be, or perceived to be, threatened and have set up strong safeguards. Detailed procedures for identifying potential threats to independence and establishing appropriate safeguards are embedded into our audit methodology. For example, staff must complete:

- an annual Code of Conduct return which confirms that they are aware of their ethical and professional obligations; and

- a declaration of independence, in advance of involvement in any audit or other public assurance engagement, which highlights where potential or actual conflicts of interest might exist. Examples could include staff members leaving to join an NAO-audited body or staff members with family members or close associates working for NAO-audited bodies.

3.7 Once safeguards are in place, they are checked regularly to ensure compliance, and teams are expected to report back promptly where circumstances change.

3.8 An ethics function supports the C&AG in discharging his role as ethics partner. It reviews each reported conflict of interest against the Revised Ethical Standard 2019, to evaluate perceived or actual threats to independence, and determine appropriate and effective safeguards. As part of the review of quality management for the introduction of the new quality framework (ISQM1), the ethics function served as a pilot area in the design and implementation of a quality risk register.

Case study

Managing ethical risks – moving from rules to risks

We are changing how we are managing quality at the NAO. In line with the ISQM1, we are moving from a system of controls to a risk-based system. We piloted this on our approach to quality management for ethics.

Quality risks around ethics include how we ensure we manage conflicts of interests when conducting audits and how we manage ethical threats, for example there is a risk an auditor may become over-familiar with audited bodies if there is not sufficient staff rotation.

As part of moving to a risk-based system, we created a detailed register to manage ethical risks. This included risks mandated by the ISQM standard but also those unique to the NAO. For example, potential conflicts for individuals with political affiliations or undertaking political activities.

Moving from a system of controls to a proactive risk-based system gave us a framework to assess our ethical risks against the quantity and quality of controls we have in place. Our biggest challenge was to create a usable risk register with ethical risks pitched at the right level. We had many discussions about whether the risks we initially highlighted were too specific or too high level to manage. As a result, we have begun a process of rebalancing our controls based on our agreed risk profile and have withdrawn mitigations from low impact and low likelihood risks and increased mitigations against ethical risks assessed as high.

We are now working to make this specific register operational, including how we use, monitor and escalate issues. We will feed our findings from this exercise into the NAO's corporate risk register before ISQM1 is rolled out in December 2022.

Investing in our talent pipeline

3.9 We are a training provider for the Institute of Chartered Accountants in England and Wales professional training scheme. We recruit talent through our successful graduate and school leaver programmes, with 60 people recruited to our graduate scheme and 13 to our school leaver scheme in 2021. Last year, 84% passed the Professional Stage examinations for the Association of Chartered Accountants (ACA) qualification at the first attempt, compared with a national average of 82%, and 85% passed the Advanced Stage examinations at the first attempt, compared with a national average of 88%.

3.10 We also recruit experienced audit professionals, and other specialists, including economists, statisticians, learning and development, and digital experts to ensure we keep pace with industry developments. We also bring in analysts to support VfM work and wider experts as we develop the breadth and impact of our insight teams.

Supporting the development of our people

3.11 We have worked on improving our focus on developing our people's skills and capabilities and enhancing the quality of people management. We have strengthened our learning opportunities, including new training for our staff, in response to heightened expectations around audit quality.

3.12 Our learning and development (L&D) team helps to develop, deliver and support learning experiences across our organisation. This has included workshops delivered virtually, a wide range of tailored e-learning, coaching, mentoring and support for action learning sets (**Figure 11** on page 51). The team works with a number of experts in topic areas and combines that with its own expertise in L&D delivery to ensure that we provide our people with the best experiences and valuable insights from within and outside of the NAO. We also moved to a new online training platform called *Thrive*.

3.13 Since February 2021, we have run a monthly pulse staff survey as a means to gather regular feedback. For details of our results and actions, please see our Annual Report. We also set out priorities and progress in becoming an exemplar organisation in our Diversity and Inclusion Strategy 2021–2025.¹²

¹² National Audit Office, *NAO Diversity and Inclusion Strategy 2021–2025*, June 2021. Available at: www.nao.org.uk/corporate-information/nao-diversity-and-inclusion-strategy-2021-2025/

Figure 11
Learning and development (L&D) highlights



Source: National Audit Office

Developing people management skills

We have run a people management skills programme since 2019 with around 65–75 staff from various grades and roles taking part each year. It went fully virtual in March 2020.

Those who have engaged with the programme have reported that it enabled them to acquire tools to better manage working relationships and has led to increased confidence and awareness. Participants said that the top skills gained were:

- *“Learning coaching skills to empower team members to come up with their own solutions” and “a more effective and conscious approach to delegation”;*
- *“The open and honest approach to managing people that the programme is based on. It gave (me) more confidence that I can have similar open and honest discussions with my performance coach and that I can create an environment for such conversations with my team.”* The majority of those responding to our survey stated that their team members also noticed improvements.

Another participant said *“I now set aside time to address different elements of people and project management alongside delivering audit work. By having focus time, I am able to apply the skills and build a better working environment for me and the team.”*

The programme included a new element, in the form of 1-2-1 coaching sessions after each workshop, to prompt participants to reflect on real and tangible behaviour changes they commit to implementing when back at work.

Developing technical skills for financial auditors

3.14 Professional accountancy training for staff is supplemented by in-house bespoke training. All financial audit staff have access to a wide range of financial audit training. In addition, we have issued mandatory assurance modules for our qualified financial auditors throughout the year in the form of Audit Skills (ASk) modules. This year mandatory modules have focused on the auditing standard on audit evidence (ISA 500) and journals testing. These modules have both had follow-up assessments to help embed the learning; and support our central evaluation of our training. We also delivered mandatory training in topics such as ethics and anti-money laundering.

3.15 All front-line staff working on audit should complete the ASk modules for their grade. Completion of mandatory training is tracked and directors in each group are responsible for ensuring compliance to ensure our audit quality is not impacted.

3.16 Individuals can also select further training based on their role and prior experience. For example:

- introduction to the revised auditing standard ISA 315 on identifying the risks of material misstatement as part of our Audit Transformation Programme (ATP);
- introduction to digital financial audit;
- introduction to the NAO's financial audit methodology for direct entrants;
- the auditing of charities;
- regularity and annual report training;
- supply and departmental accounts training;
- groups training; and
- the auditing of property valuations.

3.17 To support the implementation of our new sampling methodology for our 2021-22 audits, we issued a mandatory training module. This formed part of a blended training approach including workshops where our auditors got to engage with the supporting sample selection and evaluation forms.

Developing technical skills for wider assurance staff

3.18 Staff working on VfM studies and investigations will have audit expertise, as qualified accountants, training in accounting or with equivalent audit experience, or are specialists qualified to Masters level or equivalent in other disciplines such as economics, statistics, data science, social research and operational research. Staff can also use and develop specialist skills to support work across the office through our specialist insight teams.

3.19 To maintain the technical competence of our people we provide a range of learning and development opportunities including:

- introductory courses for graduate trainees (as part of their wider audit pathways programme) and analysts;
- ongoing support and communications to ensure that experienced practitioners access continuous professional development. For example, we provide a programme of annual assurance updates, mandatory for all practitioners, to communicate key learning or changes to our quality assurance approach. This is added to by monthly email updates and knowledge-sharing showcases that run throughout the year; and
- seminars and training in specialist topics through our hubs. For example, in 2021-22, our commercial hub held 11 seminars to share and discuss findings on topics including local authority procurement and how regulation can support better value for money.

3.20 In 2022-23, we will refresh our core training offer so that it provides more detailed support at key stages of the audit process. This will support our ongoing work to refresh our guidance as we move to a more flexible, risk-based quality management approach. The offer will cover thematic areas such as communicating impact and planning for quality, while also serving as a useful resource for anyone seeking to understand the core elements of our VfM work. This content will be reviewed and refreshed on an annual basis and will be available to all staff who work on VfM reports.

Case study

VfM showcases to share our work and learning

In 2021-22 we organised nine VfM showcases – one-hour events that support our people to share how they approach their work. We covered topics such as managing risk and quality assurance in our work, the use of international comparators, and drafting and agreeing recommendations. One showcase that focused on analytical techniques included:

- the study team for the Investigation into the Windrush Compensation Scheme shared how they had analysed the Home Office’s processing of cases through its system, using a technique called process mining. Sharing innovative approaches like this across teams builds awareness and confidence in using different analytical techniques to support audit judgements;
- another team outlined how they had provided the House of Commons Environmental Audit Committee with data analysis on storm overflows, to support the Committee’s inquiry into water quality in rivers and to set out areas for further consideration; and
- the NAO’s chief analyst set out work to develop a framework to support teams to access appropriate quality assurance on analytical techniques.

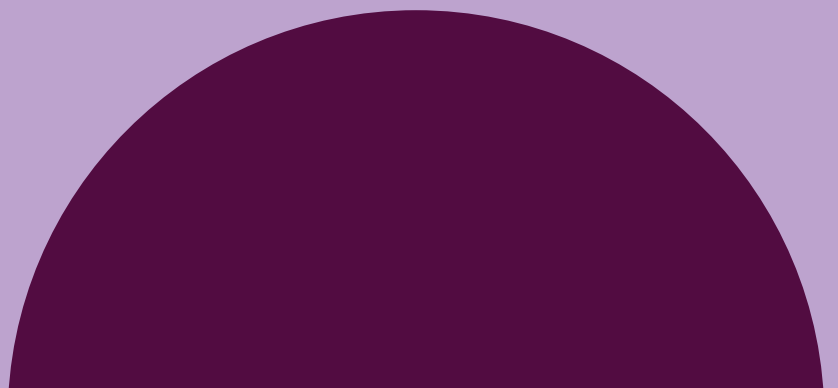
Part Four

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Governance and accountability

4.1 This part explains the National Audit Office's (NAO) governance and accountability arrangements. We describe the division of responsibility between the Comptroller and Auditor General (C&AG) and the NAO Board, and report on how governance activities have been discharged during the year.

The Comptroller and Auditor General

4.2 The C&AG, Gareth Davies, leads the NAO and is an officer of the House of Commons. He is appointed for a single non-renewable term of 10 years. He and the staff of the NAO are independent of government. We are not civil servants and we do not report to a minister.

4.3 The C&AG certifies the accounts of all government departments and many other public sector bodies. The C&AG has statutory authority to examine and report to Parliament on whether departments and the bodies they fund have used their resources efficiently, effectively and with economy. The C&AG uses his powers to:

- decide which value for money (VfM) examinations to carry out;
- decide how to report results to Parliament; and
- use rights of access to documents and staff to get information and explanations.

4.4 The NAO's Exchequer Section supports the C&AG in fulfilling his statutory Comptroller responsibilities. These responsibilities require the C&AG to approve the release of funds to HM Treasury and other public bodies, once he has satisfied himself that requests for payment are in line with relevant authorities given by Parliament.

The legal framework underpinning our governance arrangements

4.5 The NAO's governance arrangements reflect our statutory position, balancing the need for appropriate controls and oversight against the preservation of the C&AG's independence. This balance is recognised in the Budget Responsibility and National Audit Act 2011, which establishes the statutory basis for the NAO's governance. The Act modernised the NAO's governance arrangements while protecting the independence of the C&AG in matters of audit judgement. Among other things, the Act established the NAO as a corporate entity with a statutory Board led by a non-executive chair.

4.6 The Act also requires that the Board agree a Code of Practice setting out in detail how the relationship between itself and the C&AG will work in practice. In 2021-22, the chair and C&AG undertook a review of the Code to ensure that changes that have taken place over time in the NAO's operating environment remain compatible with the principles of the Code. The review led to updates to the Code, which was approved by the Board, and separately by the Public Accounts Commission (TPAC), in February and March 2022. The revised Code of Practice can be found on our website.¹³

Who holds us to account?

4.7 The NAO is accountable to Parliament through the TPAC. The role of TPAC is to:

- approve the NAO's annual budget (estimate) and lay it before Parliament;
- consider the NAO's strategy;
- appoint the non-executive members of the Board, except the NAO chair who is appointed by the Monarch via letters patent;
- appoint the external auditor of the NAO; and
- examine our Annual Report and Accounts.

4.8 During the reporting year, TPAC's remit was expanded to cover the quality of our financial audit work, as set out in paragraph 4.12. This change in remit led to a hearing in November 2021 to examine and challenge us on the quality of our financial audit work. This was followed by a hearing in March 2022 when TPAC considered the NAO's annual strategy update and approved the 2022-23 estimate. The Board concluded at its meeting in March 2022 that the added frequency of meetings with TPAC had led to a richer conversation informed by multiple data sources.

Oversight over the quality of our financial audit work

4.9 Currently, under the Companies Act 2006, the Financial Reporting Council (FRC) acts as the Independent Supervisor over our Companies Act audit work. As well as this, the C&AG invites the FRC to review the rest of our audit portfolio under a letter of engagement between the C&AG and the FRC. In May 2022, as part of the government's response to its consultation on reforming the audit profession and its regulation, the government accepted that the oversight arrangements over the quality of the C&AG's financial audits should be amended so as to better reflect the C&AG's appointment by Parliament to audit bodies under statute.¹⁴ As a result, it will legislate to transfer responsibility for arranging supervision from the FRC to Parliament.

¹³ National Audit Office, *Code of Practice dealing with the relationship between the National Audit Office and the Comptroller and Auditor General*, March 2022. Available at: www.nao.org.uk/report/relationship-between-nao-and-the-comptroller-and-auditor-general/

¹⁴ Department for Business, Energy & Industrial Strategy, *Restoring trust in audit and corporate governance: government response to consultation on strengthening the UK's audit, corporate reporting and corporate governance systems*, May 2022. Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1079594/restoring-trust-in-audit-and-corporate-governance-govt-response.pdf

4.10 In practical terms this will mean that, subject to legislation, the FRC's current statutory role over the NAO will be repealed. This will be replaced by an arrangement through which TPAC, on behalf of Parliament, will hold the C&AG to account for the quality of our work. An independent body will be appointed to inspect our work under a voluntary arrangement, and its findings will be considered by TPAC. We currently expect that these arrangements will formally take effect from April 2024.

4.11 We are working with government and Parliament, through TPAC, to take forward these proposals including the necessary changes to relevant legislation. Our aim is to be transparent and accountable for our work so that those who appoint us to undertake audits on their behalf, Parliament, are better able to hold us to account for its quality.

4.12 In preparation for this, in November 2021, TPAC piloted its new role for the first time through a session where it examined the most recent internal and external financial audit quality inspection findings. During this session (see case study), it challenged the C&AG on the NAO's responses to these findings and our plans to ensure the quality of our work meets best professional standards.

Division of responsibility

4.13 Figure 12 on pages 60 and 61 depicts the division of responsibility between the different entities involved in our governance framework.

Being held to account on audit quality

TPAC's hearing on the quality of our financial audit work in November 2021 provided a further means by which the NAO would be held to account for what it does and for being open in the way in which it does it.¹⁵

TPAC considered written evidence from the NAO including its transparency report for 2020-21, FRC's overall Report to the C&AG following its recent inspection programme, and a statement from the C&AG setting out the progress being made to further improve the quality of our work. TPAC also held a private session with the FRC's Audit Quality Review (AQR) team on its findings beforehand.

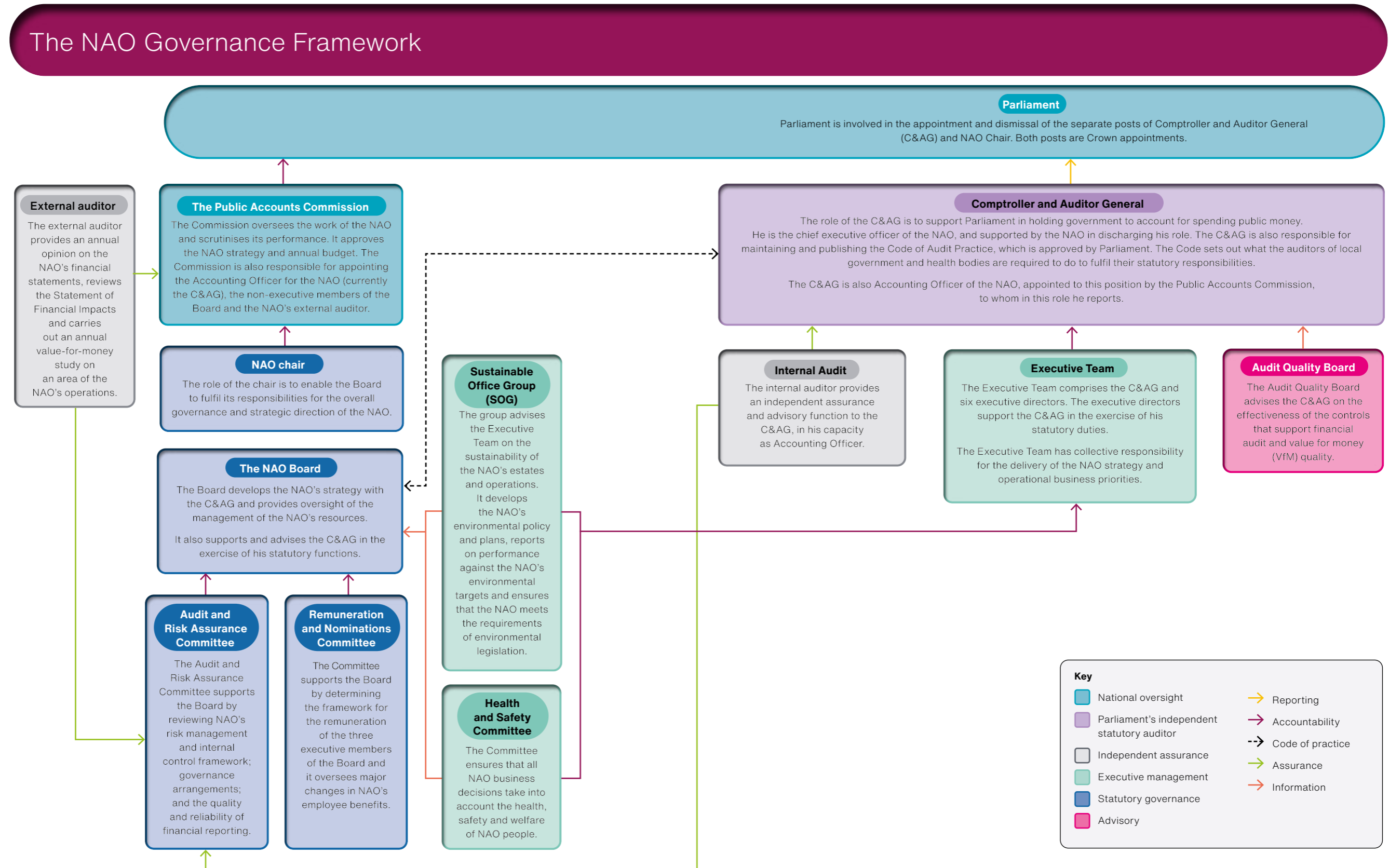
The witnesses for the November 2021 hearing were the C&AG and the two executive directors responsible for the Financial Audit service line. They were asked about the barriers that get in the way of delivering consistently high-quality audits and our progress on the initiatives to address these in our Quality Plan. TPAC focused on the areas raised in the AQR's recent inspection report and our timelines for improvement. It also challenged our progress in implementing our Audit Transformation Programme from 2022-23, as this was a key intervention which would ensure the consistent quality of our work.

This hearing was the first time an audit body was held to account before a Parliamentary select committee for the wider quality of its work, reflecting the importance Parliament places on the NAO's work. TPAC also took the opportunity in its March 2022 hearing, as one of the witnesses was the chair of the Audit Quality Board, to follow up issues first raised in the November hearing. The members of TPAC were assured that we were addressing the issues raised and had put in place the right steps to continue to improve.

It is expected that this will be an annual event and we will build on these new arrangements during 2022-23.

¹⁵ House of Commons, Public Accounts Commission, oral evidence: National Audit Office Annual Reports and Accounts, 30 November 2021, available at <https://committees.parliament.uk/oralevidence/3161/pdf/>

Figure 12
National Audit Office (NAO) governance framework



Note

1 Graphic also shows the two Board sub-committees and two committees that support the Executive Team.

Source: National Audit Office

NEXT PAGE:
The board

The Board

4.14 The role of the NAO Board is to provide effective support and challenge in improving the NAO's operations, providing additional rigour and discipline in decision-making and bringing insight from the wider experience of the non-executives to inform and shape the strategic thinking of the NAO. Importantly, it sets the tone from the top.

4.15 The Board consists of nine members: five non-executive members, including the chair, and four executive members including the C&AG who is a permanent member. Dame Fiona Reynolds has been chair since January 2021.¹⁶

Board meetings

4.16 The Board met eight times during the year, including a whole-day strategy session and a meeting to discuss the findings from its external Board evaluation. During the year, the Board:

- considered and approved the updated Code of Practice between the C&AG and the NAO;
- advised on the importance, for Parliamentary accountability, of restoring the timetable for audit certification following the disruption caused by the COVID-19 pandemic;
- challenged the Financial Audit Quality Plan, including the Audit Transformation Programme, to ensure it meets our ambitious quality objectives; and
- considered the implications of the government's sanctions on Russia on the bodies we audit and our operations at the last Board of the financial year.

Board committees

4.17 The Board has two committees to which it has delegated specific responsibilities:

- the Audit and Risk Assurance Committee, chaired by Gaenor Bagley since January 2022, is responsible for reviewing and providing assurance to the Board on the effectiveness of NAO's internal controls, risk management framework, the integrity of the financial statements, including the statement that relates to NAO's financial impact, and overseeing the external audit process; and
- the Remuneration and Nominations Committee, chaired by Dame Clare Tickell, looks at the pay and performance of the executive directors, human resources-related topics, and talent and succession planning.

¹⁶ For further details on the Board, see Comptroller and Auditor General, *Annual Report and Accounts 2021-22*, June 2022, HC 512, National Audit Office, pages 111–116. Available at: www.nao.org.uk/wp-content/uploads/2022/06/National-Audit-Office-Annual-Report-and-Accounts-2021-22.pdf. Biographies for board members are on pages 101–105 or on our website www.nao.org.uk/about-us/governance/nao-board/.

4.18 In addition, the C&AG established an advisory committee, the Audit Quality Board (AQB), to strengthen our governance and processes around quality. Its work supported the Audit and Risk Assurance Committee as that Committee considered our corporate risks relating to audit quality.¹⁷ The AQB, chaired by Janet Eilbeck, covers both financial and VfM audit quality and challenges the effectiveness of the controls we have in place supporting audit quality. It was introduced in March 2021 and, during 2021-22, the AQB met six times to advise on aspects of quality and focused on:

- the progress of the Audit Transformation Programme, including emerging findings from the six pilot audits, the timetable for wider office roll-out and having adequate support and training for this new programme;
- the control framework for our VfM work and examined plans to move to a more risk-based approach to quality assurance;
- the timetable and progress of this year's audits and ensuring audit quality while working to restore audit timetables to the pre-pandemic position;
- the progress of the annual financial quality and VfM review programmes, including key findings coming out of these reviews;
- commenting on the updated Financial Audit Quality Plan, the TPAC hearing on the quality of our financial audit work, and draft Transparency Report; and
- advising on our response to the areas that have been identified by the FRC as requiring improvement, such as work to enhance the centre of expertise on financial instruments.

4.19 The following case study outlines the benefits we have seen from the AQB's first year.

¹⁷ National Audit Office, terms of reference, Audit Quality Board, June 2022. Available at: www.nao.org.uk/wp-content/uploads/sites/13/2021/05/Audit-Quality-Board-ToR-June-2022.pdf

Value added by the Audit Quality Board

The Audit Quality Board's remit is to provide challenge and assurance to the C&AG as part of the NAO's key risk of managing the quality of all our audit work. The Board's two non-executive directors (NEDs) were key in developing its role and Janet Eilbeck, as chair of the Board, set out in her annual report where she felt it had added value to the work of the NAO:

"Our remit covers the frameworks the NAO has in place to ensure the quality of its financial and value-for-money work. We provide expert challenge and advice to the NAO on the effectiveness of its processes and to support it as it addresses the quality challenges it faces. We, therefore, not only ask difficult questions, but also observe and comment on processes in real-time.

"We have done much over the last year to educate ourselves on the quality challenges facing the NAO and how we might contribute to addressing these, for example:

- In determining our remit and terms of reference, we adopted best practice from similar boards within the bigger audit firms from our reading of their transparency reports and also having consulted privately with a couple of firms' AQB equivalents.
- I and my fellow NED met with groups of NAO audit managers to discuss their experiences and seek their feedback on what we can do to support their work.
- We challenged the progress the NAO is making in implementing its Audit Transformation Programme, including meeting with those teams adopting the new auditing standards early so we better understand the NAO's new audit risk assessment framework.

"On financial audit, the NAO is making real progress in taking forward the quality agenda. It is addressing the issues raised from its inspection programmes and needs to maintain its momentum against the increasingly higher expectations of audit quality set for the profession as a whole.

"On value for money, we contributed to the NAO's plans to improve the development of the new risk analysis of the VfM process. I am also assured that the NAO continues to deliver a quality programme of outputs across the wide complexity of government activity."

Source: National Audit Office

Executive team

4.20 The NAO's executive team is responsible for supporting the C&AG in running the NAO. It comprises the C&AG and six executive directors. Each executive director has functional responsibility, and is accountable, for the performance of an area of our work that is essential for the successful delivery of our five-year strategy. The executive directors are responsible for that function across the office. Each executive director also leads, and is accountable for, the performance of one of NAO's six groups.¹⁸

4.21 The executive team met monthly throughout 2021-22 to provide strategic and operational leadership, set goals, develop our strategy and ensure it is executed effectively, informed by high-quality management information. The team also met informally during each week, to keep each other up to date with developments in their areas of the business.

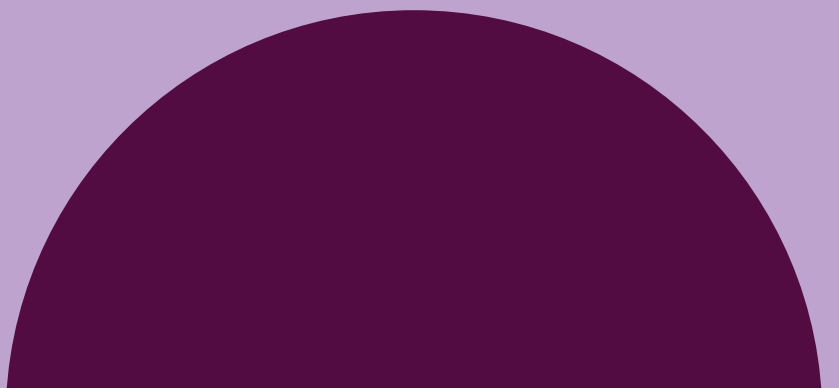
Risk management

4.22 Our risk management framework is aligned to HM Treasury's Orange Book's best practice principles. Our approach helps us to identify, assess, treat and monitor the NAO's risks. We capture our organisation-wide risks in a live corporate risk register document. The executive team receives monthly risk reporting to inform its consideration and assessment of risks. Our approach to risk management and details of our principal risks are in our Annual Report for 2021-22.¹⁹

¹⁸ See footnote 16, pages 101–105 of our annual report has biographies of the executive team, or our website at: www.nao.org.uk/about-us/governance/executive-team/

¹⁹ See footnote 16, pages 122–128 of the annual report for further details.

Appendix One



Value-for-money standards and quality approach

1 The National Audit Office's (NAO's) standards for value for money (VfM) and other wider assurance work (VfM standards) set out the expectations that all VfM studies, investigations and other wider assurance outputs must meet. Colleagues working on these types of work are expected to adhere to the standards and this is considered part of the internal quality assurance arrangements. There are 12 standards covering:

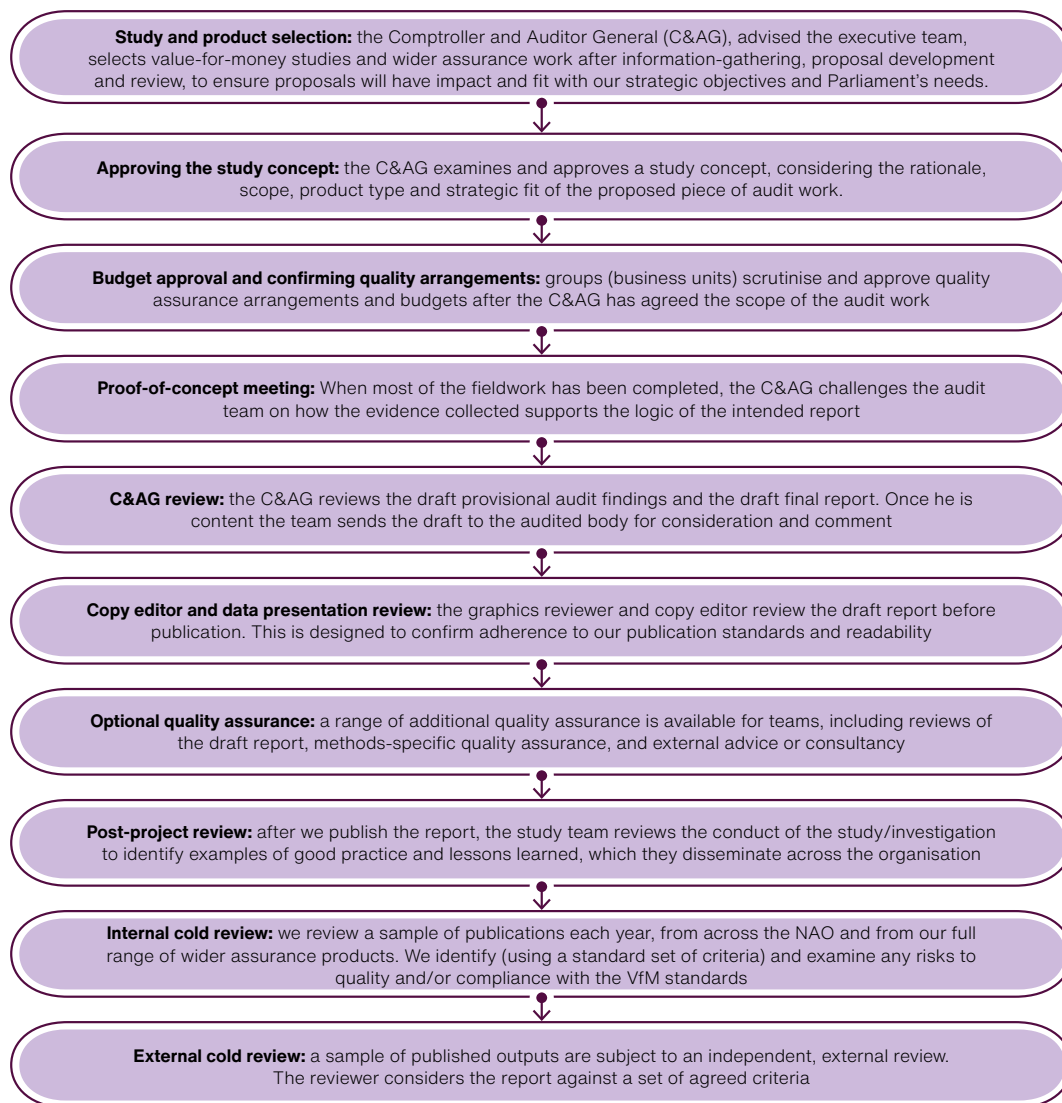
- integrity, objectivity and independence;
- proposing and selecting work;
- design and planning;
- evidence and analysis;
- forming conclusions and recommendations;
- reporting;
- quality assurance;
- project management and monitoring;
- engaging with audited bodies;
- engaging with other stakeholders;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

2 These standards are supplemented by detailed guidance relating to specific stages in the lifecycle of a VfM study, investigation and/or other type of wider assurance work, including analytical and technical methods and approaches. The guidance is held electronically and updated as and when required.

3 **Figure 13** on page 68 shows our approach to VfM quality. We have included further details of our approach in relation to value-for-money and wider assurance work in Part Two of this report.

Figure 13
National Audit Office (NAO) value-for-money (VfM) quality approach during 2021-22

Directors ensure that quality assurance arrangements are put in place for their studies and investigations. For example, for each study, there is a quality assurance plan, which is agreed by the executive director and an independent director within their group (business unit). 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 currently controlled using the following approach. We are revising this approach in 2022-23, as we describe in Part Two, paragraphs 2.59 to 2.61.

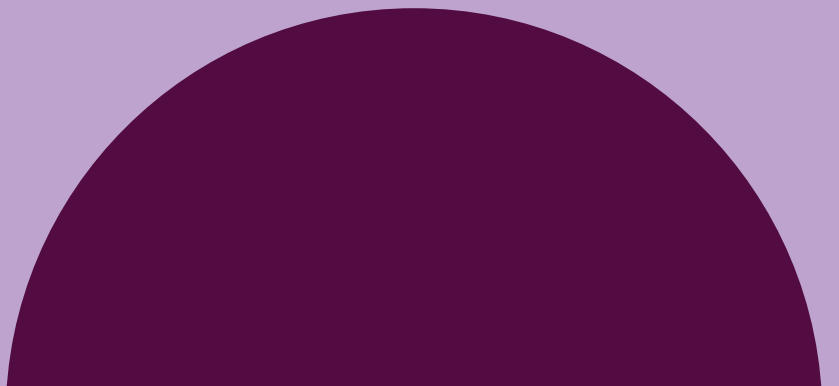


Source: National Audit Office

Appendix Two



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External quality control framework

Financial audit

1 Each year, the Financial Reporting Council (FRC) is required under statute to review our Companies Act audit work and related National Audit Office (NAO)-wide procedures. Given this, the NAO invites the FRC's Audit Quality Review team (AQR) to review, under an annual agreement between the Comptroller and Auditor General (C&AG) and the AQR, the rest of our financial audit portfolio. This means that, from the 2020-21 inspection cycle, the FRC reviews a sample of nine of our audits (an increase from seven in previous years): five of which we undertake under the Companies Act and four from the rest of our audit portfolio.

2 These reviews provide the NAO with feedback as to where we need to improve the quality of our audit work and strengthen our procedures to help support our audit teams. The work provides valuable insights as to the issues facing the wider auditing profession, of which we are part, and allows us the opportunity to benchmark our performance against the major audit firms.

3 During 2021-22, the FRC completed its reviews of our 2019-20 audits. It highlighted a number of areas where we needed to improve.²⁰ We responded promptly so audit teams could address these issues as soon as practically possible:

- **Improve our evidence as to why we are able to rely on work performed by others, including management's experts and external information sources:** we provided mandatory training to audit teams in autumn 2021 on the requirements of ISA (UK) 500 on audit evidence, covering the need to consider sources of audit evidence and the differential requirements for management experts or external information sources. Practical examples included in this training included scenarios on evidence required to support management's estimates and valuations.

²⁰ Available at: www.nao.org.uk/about-us/wp-content/uploads/sites/12/2021/09/Audit-Quality-Inspection-2020-21.pdf

- **Strengthen our challenge of the management of audited entities in areas of judgement, in particular for key assumptions used in valuations and estimates:** we have strengthened our training programme to make clearer to colleagues the importance of evidencing their consideration of such matters. As part of our implementation of ISA (UK) 540 standard on Auditing Estimates, we revised our standard audit work programmes for these areas, provided supporting guidance and mandatory training, which included specific elements on exercising professional scepticism when auditing estimates. We continue to highlight relevant findings from our inspection programmes so that audit teams can address these during their audit work. In addition, where there are areas of complexity, audit teams are required to engage with our centres of expertise to secure the most appropriate advice and capability (this might include securing advice from parties external to the NAO, such as from our framework partners) so that they will have the most appropriate evidence supporting their judgements.
- **Improve the quality of our more complex financial services audits and more complex financial services-related balances on other audits:** we have a series of actions completed, under way or planned to help address these findings. For example, we acknowledge that, at present, there is a reliance upon more generic guidance and testing procedures. This prompts teams to consider the relevant ISAs (including notably ISA 540), but we could do more to provide more tailored support to teams auditing these complex areas. As part of our Audit Transformation Programme, we will move towards a more specific articulation of risks of material misstatement, with targeted audit responses based on the level of assessed risks. In effect, this will, over time, lead to a dedicated methodology for financial services-type issues. In the meantime, as the root cause of many of the issues relates to understanding the requirements of ISAs for audit evidence, we have, as discussed above, required auditors to complete training on the application of ISA 500 to help address this concern.

Our financial instruments centre of expertise continues to develop its capacity and expertise to support teams in this area (see paragraph 2.36). This has included a new framework for commissioning external expert support, issuing guidance directly to teams (including on expected credit losses) and an increasing role in supporting consultation. The centre has developed a detailed plan of activities which aims to further strengthen our work in this area.

- **Improve our justification and explanations of key judgements around materiality:** through our quality inspection programmes, we continue to remind teams of our expectations in this area. Our new materiality toolkit requires audit teams to evidence the basis for materiality, taking into account context and user interest. We require teams to explicitly consider the range of users of the financial statements and whether we need to apply a lower materiality threshold to some areas dependent on their interest. Our full suite of audit tools and revised methodology (as part of our Audit Transformation Programme) will embed the above.

- **Improve our audit sampling procedures:** we have introduced a revised approach to audit sampling for the 2021-22 audit cycle as part of our Audit Transformation Programme. This revised approach was supplemented by detailed mandatory training in autumn 2021. Our procedures strengthen our wider approach to sampling and the importance of evidencing the justification of sample sizes.
- **Improve our consideration and testing over journal entries to respond to the risk of fraud and management override of controls:** we have provided mandatory in-depth training to all audit colleagues on identifying a journals population. This sets out clearer expectations as to the documentation and explanations required for testing. This training goes through the steps we expect teams to follow to derive the complete population of journals from the entire general ledger obtained from audited entities. Our auditors are required to justify clearly their judgements when deciding on the final journals population to be tested for the risk of fraud.

4 The FRC has recently completed its review of a sample of our 2020-21 audits. In some areas, such as materiality and sampling, the improvements we made had taken effect and the FRC identified no improvements that were required. In other areas, its findings highlight that many of the initiatives set out in our Financial Audit Quality Plan (see paragraphs 2.33 to 2.34) will not take full effect until our 2021-22 audit cycle, due to the timing of the inspection cycle. However, we consider that our plans are focused on the right areas to deliver high-quality work consistently.

5 In its recent inspection programme, the FRC set out that we need to do more to:

- take further steps to ensure consistency in **quality of more complex financial services audits**;
- improve the audit procedures over the **valuation of harder to value assets and investments**;
- improve the evaluation and challenge of management over **key judgements and estimates**, including the use of experts;
- strengthen the **framework of group auditor oversight** of component auditor work; and
- improve the consideration and testing over **journal entries** to respond to the risk of fraud and management override of controls (although findings in this area did not in themselves lead to audits receiving poorer quality ratings).

6 All these findings will continue to inform our Financial Audit Quality Plan and interventions to support our future audit work. A summary of our Quality Plan, and actions taken so far, is highlighted in Part Two (paragraphs 2.33 to 2.37).

Value for money (VfM) reports and investigations

7 For more than two decades, we have used external specialists to review our wider assurance reports. In 2021-22, a sample of 14 reports were reviewed by independent experts from RAND Europe and Risk Solutions. Our reviewers assess the report against a set of criteria covering:

- scope and rationale;
- context;
- key messages;
- synthesis of analysis;
- recommendations;
- structure and presentation;
- relevance of content;
- quantitative analysis including financial information;
- qualitative analysis;
- graphics; and
- methods.

8 Our external reviewers provide a written review assessing how each report performs against the criteria, leading to an overall assessment. This year, we have again requested a summary of the key points from across the reports reviewed, focusing on areas of particularly high quality and areas for improvement. Key findings are set out in **Figure 14** on pages 74 and 75.

Figure 14

Key findings from external cold reviews on National Audit Office (NAO) value-for-money (VfM) reports, investigations and knowledge products

Review criteria	Review comments
Scope and purpose	<p>The scope and purpose of the reports were often well described, with appropriate detail; clear explanations of often complex contexts; and good referencing to other relevant material.</p> <p>In some cases, additional information would have helped the reader to understand the rationale, purpose, timing and audience for the report – for example, to help explain why a VfM conclusion was not made in a VfM report.</p>
Context of work	<p>Reports provided good information on the wider context and could build on this more by exploring systemic issues.</p>
Key messages	<p>Summaries were generally well written, conveying the key messages in a clear and persuasive way and providing a fair and balanced reflection of the contents of the main report.</p> <p>However, reviewers felt summaries were often too long and graphics could have been used to aid understanding of complex contexts. In a few instances, more information on the scope and context of the study could also have been usefully added to the summary to help make it stand-alone.</p>
Meeting the purpose of the work, and synthesis of information	<p>Reports generally covered all the elements set out in the scope, although reviewers sometimes queried the depth and scope of the analysis in relation to the stated scope and purpose of the work.</p> <p>While reports tended to meet the purpose of the work, conclusions could be tentative. There were examples of reports using bold and confident language in the conclusions, but in some cases stronger conclusions could have been drawn.</p>
Recommendations	<p>In a few reports, the recommendations were sufficiently based on evidence, clear about responsibilities, sufficiently detailed, and could be easily monitored.</p> <p>In others, however, it was not clear if all recommendations made were feasible or how they might be put into practice. For example, some recommendations were ambitious or did not acknowledge the systemic issues.</p>
Structure and presentation	<p>The structure and presentation of the reports tended to be coherent and easy to navigate.</p>
Relevance of content	<p>The content was largely relevant to the stated scope and objectives. Some reports and summaries, however, were either overly long or lacked additional information that could have further benefited the report and its objectives.</p>
Quantitative analysis	<p>Generally appropriate and effective. In some reports more quantitative information could have been presented or been subject to greater scrutiny and analysis.</p>

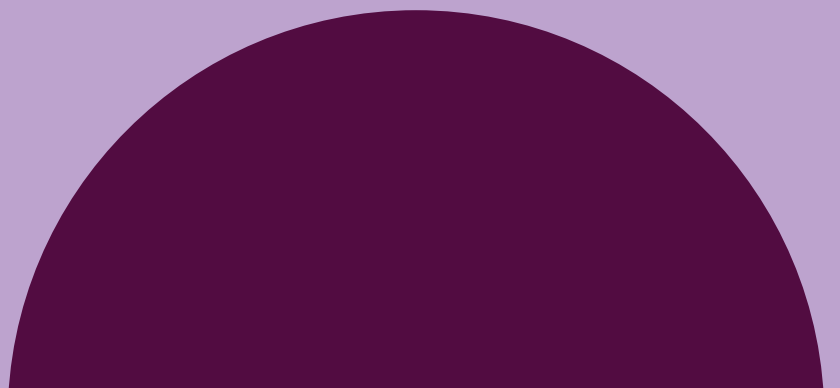
Figure 14 *continued*

Key findings from external cold reviews on National Audit Office (NAO) value-for-money (VfM) reports, investigations and knowledge products

Review criteria	Review comments
Qualitative analysis	In some reports, qualitative data could have been used more to illustrate findings. The source of opinions cited in reports is sometimes unclear and, in some instances, more systematic analysis could have been provided using NAO frameworks.
Graphics	Graphics were often used well, with a good mixture of graphs, tables, timelines and figures. Increasingly, engaging and informative infographics were included. Line graphs and bar graphs followed a common design theme and were understandable to a lay reader. There were some examples of tables and figures laid out as double page spreads, which are not readable on most computer screens.
Methods	Methodology sections needed more detail to provide confidence in the methods adopted, although there were also some examples of improved practice in methodology descriptions. In particular, reports needed more transparent and consistent information on data collection, triangulation and analysis. Some reports continued to lack sufficient discussion of the impact of limitations of the data.

Source: National Audit Office summary of findings from RAND Europe and Risk Solutions

Appendix Three



Review of effectiveness

1 As Accounting Officer, the Comptroller and Auditor General (C&AG) has responsibility for reviewing the effectiveness of the system of internal control. This review is informed by the work of the director of internal audit and assurance (DIAA), the executive directors within the National Audit Office (NAO) responsible for developing and maintaining the internal control framework, and comments made by external auditors in their management letter and other reports.

2 The DIAA's annual report concludes that the NAO has "adequate and effective governance, risk and control arrangements". The DIAA has arrived at this opinion by:

- delivering an annual operational plan for 2021-22, approved by the executive team and Audit and Risk Assurance Committee (ARAC), set against a detailed Audit Needs Assessment to prioritise activity over a three-year planning period, and designing an internal audit strategy and annual operational plan;
- consistently applying a risk-based methodology, conforming with the Public Sector Internal Audit Standards;
- delivering 22 individual assurance assignments, together with advisory support 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 reasonable.

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

4 The Board keeps its internal control arrangements under review in response to internal and external developments. The Board is independently advised by the ARAC.

Internal control weaknesses

5 There were no significant weaknesses in our system of internal controls in 2021-22 that affected the achievement of our key policies, aims and objectives.

Appendix Four

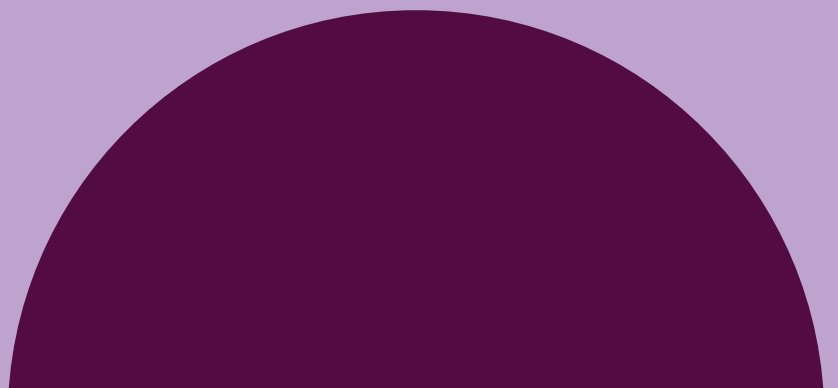


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Financial information

1 Our full financial information is contained in our Annual Report and Accounts 2021-22, which can be found on our website. **Figure 15** on page 80 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 60.3% of the National Audit Office's gross expenditure. The remainder relates to other assurance work. The Comptroller and Auditor General's comptroller function is reported as a separate segment.

Figure 15
National Audit Office operating segments

2021-22									
	Audit and assurance	Value-for-money and wider assurance work	Knowledge	Support to Parliament	International relations	Comptroller function	Voted	Non-voted	Total
	£000	£000	£000	£000	£000	£000	£000	£000	£000
Gross expenditure	71,850	17,805	7,603	5,526	699	171	103,654	293	103,947
Contract income	(22,996)	-	-	-	(271)	-	(23,267)	-	(23,267)
Other income	(1,506)	(373)	(159)	(116)	(15)	(4)	(2,173)	-	(2,173)
Net expenditure	47,348	17,432	7,444	5,410	413	167	78,214	293	78,507

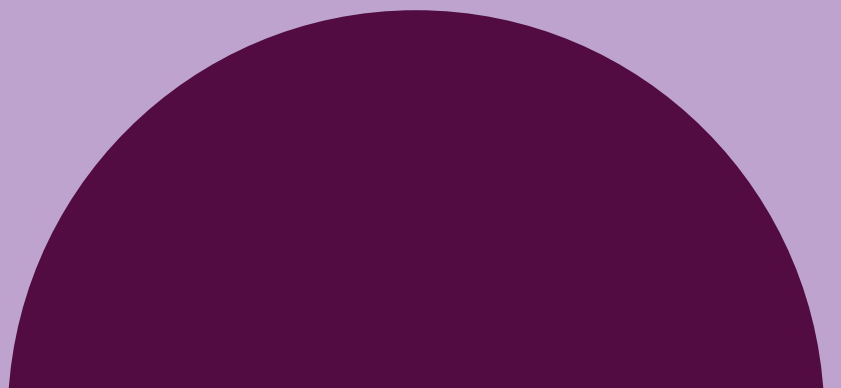
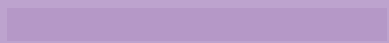
2020-21									
	Audit and assurance	Value-for-money	Investigations and insight	Support to Parliament	International relations	Comptroller function	Voted	Non-voted	Total
	£000	£000	£000	£000	£000	£000	£000	£000	£000
Gross expenditure	67,469	16,671	8,239	5,117	829	126	98,451	293	98,744
Contract income	(21,858)	-	-	-	(44)	-	(21,902)	-	(21,902)
Other income	(1,847)	(457)	(226)	(140)	(23)	(3)	(2,696)	-	(2,696)
Net expenditure	43,764	16,214	8,013	4,977	762	123	73,853	293	74,146

Notes

- Voted expenditure and income is allocated to the National Audit Office (NAO) by a Parliamentary vote each year through the Supply and Appropriation Act. The NAO reports the use of this expenditure and income under its main operating segments about which further information can be found in the Performance Report on pages 88 to 93 of NAO's Annual Report and Accounts 2021-22. Our value-for-money and wider assurance work now includes our response work, which was previously known as investigations and on which we spent £1.8 million in 2021-22 (2020-21: £1.4 million). Our knowledge objective which replaces 'insight' now focuses on our plans to invest in our knowledge management processes and systems, and provide specific expertise to support reports and activities, drawing together lessons learned for our audited bodies and Parliament.
- Non-voted expenditure comprises the Comptroller and Auditor General's and chair's salaries and is paid directly from the Consolidated Fund. This is outside of the control of the NAO and is not subject to the same annual Parliamentary approval process.
- Contract income 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. Other income cannot be directly attributed to the NAO's operating segments and has been apportioned between them in line with gross expenditure.
- The chief operating decision body of the NAO is considered to be the executive team and details of its membership can be found on page 101 of the Annual Report and Accounts. Due to the integrated nature of the NAO's activities, it is not possible to distinguish meaningfully between assets and liabilities attributable to the different operating segments and therefore the executive team does not receive information on assets and liabilities by operating segment. For this reason, in line with IFRS 8 (Operating Segments), no such analysis is presented here.

Source: National Audit Office

Appendix Five



Transparency report disclosure requirements

1 Figure 16 on pages 83 to 85 sets out National Audit Office compliance with disclosures required by Article 13 of Regulation (EU) 537/2014 to produce an annual transparency report.²¹

²¹ It forms part of the law of England and Wales, by virtue of section 3 of the European Union (Withdrawal) Act 2018, and as amended by the Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2019/177.

Figure 16

How the National Audit Office (NAO) complies with the disclosures required by Article 13 of Regulation (EU) No 537/2014

Provision of Regulation (EU) 537/2014	How the National Audit Office complies with Regulation (EU) 537/2014
<p>A description of the legal structure and ownership of the statutory auditor, if it is a firm.</p>	<p>The Comptroller and Auditor General (C&AG), Gareth Davies, leads the National Audit Office (NAO) and is an officer of the House of Commons, as established by statute. He and the staff of the NAO (911 full-time equivalent permanent staff) are independent of government. They are not civil servants and do not report to a minister.</p>
<p>Where the statutory auditor or the audit firm is a member of a network:</p> <p>(i) a description of the network and the legal and structural arrangements in the network;</p> <p>(ii) the name of each member of the network that is eligible for appointment as a statutory auditor, or is eligible for appointment as an auditor in an European Economic Area (EEA) State or in Gibraltar;</p> <p>(iii) for each of the members of the network identified under paragraph (ii), the countries in which they are eligible for appointment as auditors or in which they have a registered office, central administration or a principal place of business;</p> <p>(iv) the total turnover of the members of the network identified under paragraph resulting from statutory audit work or equivalent work in the EEA States or Gibraltar.</p>	<p>N/A. The NAO is a Supreme Audit Institution and not part of a network.</p>
<p>A description of the governance structure of the statutory auditor, if it is a firm.</p>	<p>The NAO's governance structure is shown in Part Four.</p>
<p>A description of the internal quality control system of the statutory auditor and a statement by the management body on the effectiveness of its functioning.</p>	<p>Part Two sets out a description of the NAO's internal quality control system. 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.</p>
<p>An indication of when the last quality assurance review referred to in Article 26 of Regulation (EU) 537/2014 was carried out.</p> <p>A list of public interest entities for which the statutory auditor carried out statutory audits during the preceding financial year.</p>	<p>Such reviews are undertaken annually. We have set out details of this review in Part Two and Appendix Two.</p> <p>In 2021-22, the NAO audited four public interest entities:</p> <ol style="list-style-type: none"> 1 Network Rail Infrastructure Finance PLC 2 CTRL Section 1 Finance PLC 3 LCR Finance PLC 4 HM Treasury UK Sovereign SUKUK PLC
	<p>The NAO continues to audit NRAM Limited, which was previously categorised as public interest entities, but no longer currently meets the relevant criteria.</p>

Figure 16 *continued*

How the National Audit Office (NAO) complies with the disclosures required by Article 13 of Regulation (EU) No 537/2014

Provision of Regulation (EU) 537/2014	How the National Audit Office complies with Regulation (EU) 537/2014
A statement concerning the statutory auditor's independence practices which also confirms that an internal review of independence compliance has been conducted.	See Part Three 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 2021-22.
A statement on the policy followed by the statutory auditor concerning the continuing education of statutory auditors referred to in paragraph 11 of Schedule 10 to the Companies Act 2006.	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 Three for further detail of these policies and practices.
Information concerning the basis for the remuneration of members of the management body of the statutory auditor, where that statutory auditor is a firm.	The NAO is not an audit firm and has no partners. For details of remuneration, see our Annual Report and Accounts.
A description of the statutory auditor'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, subject to some approved exceptions although for no longer than seven years. Also, we ensure that other team members are not involved in an engagement for more than seven years.
Where not disclosed in its accounts, information about the total turnover of the statutory auditor, divided into the following categories:	<p>Most audits the NAO undertakes are funded by Parliament. In these cases, the organisations we audit must reflect the notional cost of our audit work as operating costs within their financial statements, although no cash payment is made to us. The NAO also reports on the collection of revenues raised on behalf of government by the BBC, the Driver & Vehicle Licensing Agency and HM Revenue & Customs, including on the administration of Scottish and Welsh income tax. The cost of this work is also financed through our Parliamentary funding.</p> <p>The NAO charges cash fees for certain other financial audit assignments. This relates to the work we undertake under the Companies Act 2006 (referred to as our role as 'statutory auditor'), other statutory requirements (audits we undertake under other statute), and agreement audits. We also receive other income, largely from tenants occupying our main building. Our cash fees for these audit assignments and other services are recorded as income in the NAO's Statement of Comprehensive Net Expenditure and disclosed in Note 6 of the NAO's Annual Report and Accounts which is available on our external website. The following sets out the cash fees we have accounted for during 2021-22.</p>
(i) revenues from the statutory audit of accounts of public-interest entities and members of groups of undertakings whose parent undertaking is a public-interest entity;	(i) £0.06 million
(ii) revenues from the statutory audit of accounts of other entities;	(ii) £20.3 million

Figure 16 *continued*

How the National Audit Office (NAO) complies with the disclosures required by Article 13 of Regulation (EU) No 537/2014

Provision of Regulation (EU) 537/2014	How the National Audit Office complies with Regulation (EU) 537/2014
<p>(iii) revenues from permitted non-audit services to entities that are audited by the statutory auditor; and</p>	<p>(iii) £3.3 million. Of this:</p> <p>£0.9 million relates to other assurance engagements, including EU Agricultural Funds (£0.8 million) and the audit of interim financial statements and special purpose accounts of a small number of companies.</p> <p>£0.7 million relates to rent and service charge income from three bodies that we audit which rent office space in our London Headquarters building from the NAO.</p> <p>£1.7 million relates to fees raised on behalf of, and passed onto Audit Scotland, Wales Audit Office, and Northern Ireland Audit Office in connection with EU Agricultural Funds work.</p> <p>The NAO provides capacity building services to other Supreme Audit Institutions and receives funding to cover the costs of this work. The funding can come from a variety of sources including from government bodies. In 2021-22, the NAO received £125,581 from the Foreign, Commonwealth & Development Office (2020-21: £82,543).</p>
<p>(iv) revenues from non-audit services to other entities</p>	<p>(iv) £1.8 million, of which £1.5 million relates to rent, from non-audited entities, service charges and miscellaneous income.</p>

Source: National Audit Office

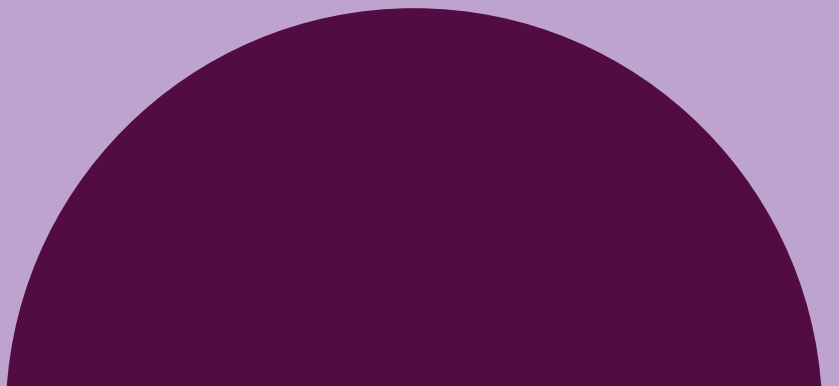
Appendix Six



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Review of National Audit Office compliance with the Audit firm governance code (Revised 2016)

- 1** The National Audit Office (NAO) is 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. The NAO does not audit listed entities.
- 2** 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 in **Figure 17** on pages 88 to 93 how we comply with the relevant provisions of the Audit firm governance code.
- 3** Throughout the code, reference to 'a firm' means a firm that audits listed companies in the UK.

Figure 17

Review of National Audit Office (NAO) compliance with the Audit firm governance code (Revised 2016)

	Provision of the code	How the NAO complies with the code
A Leadership	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.	This principle does not directly apply to the NAO. The Comptroller and Auditor General (C&AG) has statutory powers given by Parliament.
	A.1.1: The firm should establish board or other governance structures, with matters specifically reserved for their decision, to oversee the activities of the management team.	All other provisions are covered by Part Four and relevant sections of our Annual Report and Accounts 2021-22 available on our external website.
	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.	This is covered in Part Four of the Transparency Report and in the NAO’s Annual Report and Accounts 2021-22.
	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.	Covered in Part Four of the Transparency Report. Also see the NAO’s Annual Report and Accounts 2021-22, Governance Statement. Meeting attendance record is noted on page 122 of the Annual Report and Accounts.
	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 C&AG is appointed for a fixed, non-renewable term of 10 years. The non-executive members of the Board are appointed for a three-year term, renewable for one further three-year term. Executive members of the Board are appointed each year by the non-executive members, renewable annually. The chair of the Board evaluates the performance of the non-executive members of the Board. The C&AG evaluates the performance of the executive team. The performance of the chair is evaluated by the senior independent director.
	A.2: Management principle – A firm should have effective management which has responsibility and clear authority for running the firm.	The Budget Responsibility and National Audit Act 2011 (Part 2, Schedules 2 and 3) makes provision for a Comptroller & Auditor General, and National Audit Office. We comply fully with requirements. The management team’s terms of reference are set out in the NAO’s Annual Report and Accounts 2021-22, and in this Transparency Report.
	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. The NAO’s external strategy is also published online.
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. Our values are set out in Part One of the Transparency Report.

Figure 17 *continued*

Review of National Audit Office (NAO) compliance with the Audit firm governance code (Revised 2016)

	Provision of the code	How the NAO complies with the code
	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.	All NAO people, including the non-executive members of the Board, complete a Code of Conduct return annually.
	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.	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.
	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, and to the extent that the Code is relevant to the NAO as 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 set out in Part One of this Transparency Report.
C	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.	This provision does not apply to the NAO given the C&AG's statutory independence as set out in the Budget Responsibility and National Audit Act 2011. Part Four of the Transparency Report highlights our Board structure and our Annual Report and Accounts 2021-sets out the details of the NAO's Board members, including our independent non-executives and their significant and relevant experiences.
Independent non-executives	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

Figure 17 *continued*

Review of National Audit Office (NAO) compliance with the Audit firm governance code (Revised 2016)

	Provision of the code	How the NAO complies with the code
	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 due to the C&AG'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 with which 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 available on our website.
	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 section 24 of the Budget Responsibility and National Audit Act 2011.
	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.	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 Transparency Report 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.
	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's <i>Financial Audit Manual</i> 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.	Individuals supervising, managing or directing a financial audit usually hold a relevant 'audit licence'. One of the criteria for being granted a general audit licence is having undertaken appropriate continuing professional development in the previous year. This includes completion of the NAO's assurance update training which covers group audit requirements to comply with applicable standards.

Figure 17 *continued*

Review of National Audit Office (NAO) compliance with the Audit firm governance code (Revised 2016)

Provision of the code	How the NAO complies with the code
<p>D.1.3: The firm should state in its transparency report how it applies policies and procedures for managing potential and actual conflicts of interest.</p>	<p>The NAO 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 HR of any possible conflict of interest as soon as it becomes apparent during the year. See 'ethics' section in Part Three of the report.</p>
<p>D.1.4: The firm should take action to address areas of concern identified by audit regulators in relation to the firm's audit work.</p>	<p>See Part Two: External review – financial audit</p>
<p>D.2: Risk management principle – A firm should maintain a sound system of internal control and risk management over the operations of the firm as a whole to safeguard the owners' investment and the firm's assets.</p>	<p>These provisions are covered in Part Four and Appendix Three.</p>
<p>D.2.1: The firm should, at least annually, conduct a review of the effectiveness of the firm's system of internal control. The review should cover all material controls, including financial, operational and compliance controls and risk management systems.</p>	<p>See Appendix Three.</p>
<p>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.</p>	<p>See Appendix Three.</p>
<p>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.</p>	<p>The director of internal audit and assurance (DIAA), 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 2021-22 annual report and accounts is also informed by the work of the NAO's executive directors who are responsible for developing and maintaining the internal control framework, and comments made by the external auditors in their management letter. The NAO's risk management framework is aligned to HM Treasury's Orange Book.</p>
<p>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.</p>	<p>These provisions are covered in Part Three, as well as the Annual Report and Account 2021-22.²²</p>

²² Comptroller and Auditor General, *Annual Report and Accounts 2021-22*, HC 512, National Audit Office, June 2022. Available at: www.nao.org.uk/wp-content/uploads/2022/06/National-Audit-Office-Annual-Report-and-Accounts-2021-22.pdf

Figure 17 *continued*

Review of National Audit Office (NAO) compliance with the Audit firm governance code (Revised 2016)

	Provision of the code	How the NAO complies with the code
	D.3.1: The firm should disclose on its website how it supports its commitment to the professionalism, openness and risk management principles of this Audit firm governance code through recruitment, development activities, objective setting, performance evaluation, remuneration, progression, and other forms of recognition, representation and involvement.	The NAO does not need to publicly commit to the Audit firm governance code due to the NAO's unique statutory position. This 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: Whistleblowing principle – A firm should establish and apply confidential whistleblowing 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. Further details in Part Three of this report.
	D.4.1: The firm should report to independent non-executives on issues raised under its whistleblowing policies and procedures and disclose those policies and procedures on its website.	The report on any issues raised under our whistleblowing policies is a permanent agenda item for the Audit Committee meetings. The whistleblowing policy is published on our website. ²³
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 2021-22 published on our website. ²⁴
	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

²³ Available at: www.nao.org.uk/about-us/contact-us/whistleblowing/

²⁴ See footnote 22.

Figure 17 *continued*

Review of National Audit Office (NAO) compliance with the Audit firm governance code (Revised 2016)

	Provision of the code	How the NAO complies with the code
	E.4: Governance reporting principle – A firm should publicly report how it has applied in practice each of the principles of the Audit firm governance code excluding F.2 on shareholder dialogue and F.3 on informed voting and make a statement on its compliance with the Code’s provisions or give a considered explanation for any non-compliance.	This Transparency Report provides the disclosures required by this section of the Code and is available on our website. ²⁵
	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 and Risk Committee’s terms of reference are published on our website ²⁶ including membership. The Committee publishes a short description of how it has discharged its duties in the Annual Report and Accounts.
F Dialogue	F.1: Firm dialogue principle – A firm should have dialogue with listed company shareholders, as well as listed companies and their audit committees, about matters covered by this Audit firm governance code to enhance mutual communication and understanding and ensure that it keeps in touch with shareholder opinion, issues and concerns.	The NAO conducts regular meetings with senior management and we undertake internal and external dialogue. The NAO does not need to publicly commit to the Audit firm governance code due to the NAO’s unique statutory position.
	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 due to 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

²⁵ Available at: www.nao.org.uk/about-us/governance/transparency/

²⁶ Available at: www.nao.org.uk/wp-content/uploads/2022/08/Audit-and-Risk-Assurance-Committee-March-2022.pdf