



HOUSE OF COMMONS

# Public Accounts Commission

Oral evidence: [National Audit Office Supplementary Estimate 2023/24](#)

Wednesday 24 January 2024

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Members present: Clive Efford (Chair); Dame Meg Hillier; Mrs Sharon Hodgson.

Questions 1-54

## Witnesses

**I:** Dame Fiona Reynolds CBE, Chair, National Audit Office, Gareth Davies, Comptroller and Auditor General, National Audit Office, Daniel Lambauer, Executive Leader, Strategy and Resources, National Audit Office.



## Examination of witnesses

Witnesses: Dame Fiona Reynolds CBE, Gareth Davies and Daniel Lambauer.

**Chair:** Welcome to today's meeting of the Public Accounts Commission on the NAO's supplementary estimate for 2023-24. Will the witnesses introduce themselves for the record?

**Gareth Davies:** Good morning. I'm Gareth Davies, Comptroller and Auditor General.

**Dame Fiona Reynolds:** I'm Fiona Reynolds, chair of the board at the National Audit Office.

**Daniel Lambauer:** I'm Daniel Lambauer, executive director, strategy and resources.

Q1 **Chair:** You may have noticed that I'm not Richard Bacon—although I did my best to disguise myself. Unfortunately, he has had an operation, so will not be around for a short while, so I have been asked to stand in this morning. Welcome, by the way.

Of the supplementary estimate, £1 million relates to the increases in the NAO's audit work prompted by machinery of government changes. What specifically are the implications for your financial audit work of last year's machinery of government changes? Will the additional costs be one-off or transitional? Are you recruiting a further 10 full-time equivalent staff, and does this reflect a permanent uplift in the NAO's headcount?

**Gareth Davies:** As you will remember, the machinery of government changes were announced right at the end of the financial year, taking effect from 1 April. Their effect was to create three Departments where previously there were two. The very large BEIS Department and the Department for International Trade became three new Departments—essentially breaking up the old BEIS into three more manageable chunks, and combining trade with international trade. That created three Departments. From a financial audit point of view, that means that we have three sets of accounts rather than two.

The first reason why that is more work is that there is a fixed cost to auditing any large set of accounts, so we have three sets of those fixed costs rather than just two, another audit committee to attend, another audit plan to devise and so on.

The second reason is: if you take the old BEIS and split it into three chunks, that on its own creates significantly more audit work, because behind all our sample testing of expenditure and so on is the concept of materiality. Our audits are designed to make sure that there are no material errors in the accounts. Materiality is a percentage of the expenditure of the Department.



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If we have the same amount split into three chunks, smaller errors are now material to those accounts, so we have to do more testing, even though the overall amount of expenditure is the same as it was before, just divided up into smaller amounts. The impact of materiality is therefore significant—that is the biggest single driver of more work in these cases—so combining all that leads to the increase in workload that we set out in this document.

Clearly, we have already started these audits—they started in the last financial year—and we will be concluding them in this financial year. To cover that, we set out the staffing implications and yes, we are recruiting the additional staff that we set out, so we have increased the graduate intake that we have every September—because we knew this was coming, we increased that beyond our original plan—and made some direct recruitment higher up the skill mix, to make sure that we have the right skill mix in the team to do the work. For all those reasons, we have the additional resources in the plan.

**Q2 Chair:** Is the £1 million you are requesting for this work the entire cost, or was any of the additional cost absorbed in your existing budget?

**Gareth Davies:** It is the whole extra cost to us. We try to absorb it. If we hit small increased amounts of work in a year, we try to accommodate that within our previous budgets. The £1 million represents the amount that it is just not possible to squeeze out of what we already had in the previously agreed estimate for the year.

As we explained, it is not just the financial audit resources. We have also planned for sufficient value for money assurance coverage of the three new Departments. In fact, we already have work under way in all three of those Departments on the value for money side as well, so a smaller proportion of the additional resources is for that work.

**Q3 Chair:** Forgive me if I am being dim here, but I did not hear a yes or a no. Is the £1 million the full cost of the additional work that you have had to take on, or have you absorbed some of it, so the actual cost is bigger than £1 million?

**Gareth Davies:** It is the full cost of the extra work. We already had an amount in for these previous—

**Q4 Chair:** So you have absorbed nothing within your existing budget; it is all extra expenditure.

**Gareth Davies:** This is the amount that it was just not possible to accommodate. The easiest thing is to say that we have calculated the additional cost created by the split of the previously big Department into new ones, and this is the full amount of additional cost that we could not cover from our previous budget.

**Q5 Chair:** Okay. On external expertise, are you commissioning external expertise that you do not currently have, for example? In the longer term, are those the skills you are looking to build in-house? Is that your aim in what you are doing with the skills you are looking for in this



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process?

**Gareth Davies:** We need additional expertise for all our work, not just the amount created by the machinery of government changes, so perhaps I will answer the general point about why we need external expertise to carry out our work. The way that accounting and auditing standards have developed in the last few years has put significant focus on things like technical estimates and valuations in the accounts. It so happens that in those particular areas, there were significant numbers.

For example, the former BEIS Department was where the Government accounted for the bounce back loans portfolio from the pandemic, and a very substantial estimate is in there for how much of that is going to fall due to the Government, because of the guarantees that the Government made to the banks who made those loans. That estimate on its own is a very significant accounting estimate in the new Department, which is Business and Trade. So we absolutely need external expertise to help us assess the validity, the accuracy, of the estimate made by Government for that bill coming from the guarantees.

That is just one example of where external expertise is necessary for us to meet auditing standards. We also have to do that on property valuations, pension fund deficit valuations from actuaries, and those kinds of technical areas where at the moment there is no actuarial team of specialists in the NAO and no property valuation team in the NAO. These are areas we are keeping under review, because they have become much more significant parts of public sector audit than they used to be, and so there may well come a point when it is economic for us to have our own experts in-house, rather than to pay the fees of external experts in the way that we do now. That is a topic we are keeping under close review.

**Q6 Chair:** You also say that you have increased the scope of your value for money work, and that you will publish two further value for money reports. Could you provide us with some additional detail on that?

**Gareth Davies:** Yes. I have the information here. This morning, for example, we have published our report on the new Department for Net Zero, which is focused on the public subsidies to the biomass industry. That is an example of an early piece of work that will have previously been under the BEIS Department but is now under the new DESNZ Department.

We have started some work on the new Department for Science, Innovation and Technology that we will be publishing in the spring, which is on the Government's approach to artificial intelligence. We may well have done this kind of work before, but because there are now three Departments overseeing these areas, we need to give Parliament adequate coverage of all three, hence the additional resource that we have set aside. We have set ourselves the target of producing two more reports a year than we were previously.

**Q7 Dame Meg Hillier:** Just to pick up on the machinery of government changes, Comptroller and Auditor General, you said that the £1 million is the bit that you could not already absorb. What is the total cost of the



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machinery of government changes? Have you got a calculation for that?

**Gareth Davies:** To the NAO?

**Dame Meg Hillier:** Yes.

**Gareth Davies:** I think we have been able to absorb the rest in our ordinary operations.

Q8 **Dame Meg Hillier:** Have you got a figure for it even though you have had to absorb them?

**Gareth Davies:** No. The amounts that I have been describing so far will be ongoing, because these audits will continue into the future and need the additional recourse built into our budget. The one-off amount is essentially the technical issue that the previously audited figures from the BEIS accounts are now disaggregated and have become the prior year comparators. We are going to have to reaudit those numbers, even though they already have been audited. That is the only example of a one-off amount, which we do not think is significant enough—

Q9 **Dame Meg Hillier:** This is the point I am driving at. Let us be honest, politicians come in, we have a manifesto-writing season coming, and machinery of government changes become popular. Is there any figure you can put on the cost of machinery of government changes?

**Gareth Davies:** I have only been talking about the cost to the NAO of auditing these organisations.

**Dame Meg Hillier:** That is one of the costs of it.

**Gareth Davies:** We have not done an estimate for this particular one. There has been previous NAO work on machinery of government changes, which highlighted that the cost was always underestimated. Of course, the practical burden of that falls on the teams who are setting up the new arrangements because they are, essentially without additional resource, attempting to do something that takes significantly more effort than continuing to run their old Departments. We have definitely seen the capacity strain on the civil service for managing those changes. But no, we do not have an estimate of the cost of this particular change at this stage.

Q10 **Dame Meg Hillier:** So this one-off cost is just one of those extra costs of these machinery of government changes.

**Gareth Davies:** Yes.

Q11 **Dame Meg Hillier:** Okay. It is helpful to have that on the record. One of the other areas where you have asked for additional money is the work to complete audits, where unavoidable and additional costs had been incurred that had not been foreseen. Can you tell us which audits are affected by that?

**Gareth Davies:** There are quite a few, actually. Again, there is a materiality point here for us. In the normal course of an audit, there are overs and unders—as we would call them—that you generally manage

within the agreed budget for the year. Here, we are talking about where there is an exceptionally large difference. It is usually created by an issue emerging that we were not aware of at the planning stage, so it did not find its way into our budget. It emerges during the audit and requires a substantial audit response. That is often the kind of external expertise being commissioned that I was describing earlier.

We have had quite a few examples—more than our usual this year—and part of this is what I was describing earlier. The changes in accounting and auditing standards have increased the expectation on both the Government in preparing the accounts and us in auditing them. There is a higher standard of evidence for estimates and judgments made that have a significant financial impact.

There are many of those across Government. For example, we were hoping to complete our audit of the UK Health Security Agency, which is part of the Department of Health group, and sign it off this week, along with the rest of the DHSC group, but that was heavily complicated this year by the inclusion of a complex model for the supply of vaccine for the first time in the UKHSA accounts. That was previously held by the Department of Health centrally and then transferred to UKHSA part way through the year. It has turned into a very significant accounting challenge for the organisation to use the outputs of this spreadsheet to value its stock.

The issue with vaccine stock is that, first, it is very material to the accounts, and secondly, it has a shelf life. You have to estimate how much of this will become unusable, and therefore impaired in the accounts, before it can be given to the public. So that one model created very significant extra audit work for us this year and is a really good example of the kind of thing we are talking about here.

**Q12 Dame Meg Hillier:** There may be a lesson for Government there. I know from the Public Accounts Committee and elsewhere that the UKHSA was set up part-way through a financial year, which was a complication. Those complications are now being compounded by other things being done part-way through a financial year. It sounds like there are technical issues anyway, but would it have been less costly if it had been done in line with financial years?

**Gareth Davies:** Yes, that is certainly one of the complications. The other is this materiality point, on which I am a bit of a broken record. The model, previously held by the Department of Health, was barely material to the whole departmental group—

**Dame Meg Hillier:** Because it is such a big Department.

**Gareth Davies:** But it is 50 times the materiality level for UKHSA, so it becomes a very significant audit issue.

One of my observations would be that there is an issue about the overall governance of that process of moving functions around departmental groups—there has been a lot of that particularly, obviously, in DHSC—and



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fully understanding all the implications of these changes, both their timing and their nature, as well as the impact on the organisations they are moving to. I think that has been underestimated.

- Q13 **Dame Meg Hillier:** I am feeling I need to have a conversation with the Treasury Officer of Accounts about how some of this is handled. You do not need to go into this in detail, but are there other examples where this additional work has been a problem?

**Gareth Davies:** We needed some specialist evaluation advice in auditing the Government Property Agency. The Government has been quite successful in aggregating more of its Government-owned property into the agency so that it is managed in a better-value way. That now has a very large portfolio, with some very material figures in there from property evaluation estimates. We have had to commission new areas of advice on those estimates from the ones we expected to need at the start of the audit. That is another area that has added over £100,000 to our costs.

- Q14 **Dame Meg Hillier:** That is because the GPA has been successful at bringing more property in.

**Gareth Davies:** Yes, and more than anyone anticipated at the time.

- Q15 **Dame Meg Hillier:** More than they anticipated, and therefore more than you anticipated. So that was unforeseen. Anything else?

**Gareth Davies:** There are various issues around the quality of information underlying some of these complex models. That came up in the Nuclear Decommissioning Authority. It has come up at FCDO. It is unpredictable where these things will arise. It is not always a comment on the way it is being managed in the Department. Often, they couldn't have been predicted in advance and they need work from both the organisation and from us as the auditors.

- Q16 **Dame Meg Hillier:** There are those complexities, but there are also the complexities because of the changes, for example, in the valuation of land and buildings under the new audit rules. That is about £0.2 million. Surely those have been discussed a lot in the audit world. Why was that a surprise?

**Gareth Davies:** Largely, yes—we knew it was coming, so it was not the arrival of it that was the issue. Actually, some Departments went early, so we have had the benefit of early adoption, from which we then obviously transferred our learning across. You only really know when you look at the detailed figures underlying the first attempt to compile these figures under IFRS 16. In a couple of cases, that proved more challenging than we expected. We did not have the depth of information that we needed.

- Q17 **Dame Meg Hillier:** From the Department you were auditing?

**Gareth Davies:** Yes, from the Department.

- Q18 **Dame Meg Hillier:** So where does the issue lie? Is it with them or with you?





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**Gareth Davies:** Essentially, it is learning what the level of evidence required is for this new accounting basis for Government assets. Of course, we worked with all the Departments in advance, trying to share information about what was needed and case studies from where it had been done early, and that largely worked pretty well. These are just the exceptional cases where they didn't have the information that was needed first time round.

Q19 **Dame Meg Hillier:** Can you give an example?

**Gareth Davies:** I can write to you with that. I don't have the list—

Q20 **Dame Meg Hillier:** Okay. I am keen to know how to make sure that you have learned from this as these new accounting standards roll out. Supplementary estimates are unsatisfactory—I think you would agree with that. We do not want to be here again in a year's time, having the same discussion.

**Gareth Davies:** Not on IFRS 16—absolutely. I cannot rule out things that we don't know about now, by definition. On IFRS 16, I think it has been adopted pretty successfully across Government. In this small number of cases where there was more work than expected, we are pretty confident that that will not recur for next year.

It is absolutely right to say that on these known issues, we should not have more than an implementation issue, and then have it fixed. With the Environment Agency, for example, it is not a function of a new requirement this year, but it has taken them several years to have the information about their operational assets—flood defences and so on—in a state that can support a clean opinion on the accounts. In that case, that is taking three or four years to get to that stage. It depends on the scale of the task needed to make sure the records and valuations are in place.

Q21 **Dame Meg Hillier:** You are basically saying that Whitehall has got there now?

**Gareth Davies:** On IFRS 16, we think that has gone pretty well, actually.

Q22 **Dame Meg Hillier:** I know that local authorities are worrying about that, but it is a discussion for another day. If you have the supplementary estimate, will this mean that you will get all the accounts in before summer recess for sign-off?

**Gareth Davies:** This is, of course, for the financial year that is just ending. I mentioned that we were signing off the Department of Health and Social Care this week. That is the last of the Government Departments to have its 2022-23 audits completed. The bulk of them were done before the last summer recess.

Q23 **Dame Meg Hillier:** There is going to be no flow over to any of your deadlines for this summer's accounts, for 2023-24?

**Gareth Davies:** For 2023-24, the financial year that is coming to an end in March, we are hoping to increase the proportion further that are audited by this coming summer recess. I am not talking about Departments here;





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I am talking about all 408 public bodies that we audit. We went up from 53% to 60% last summer, and we are aiming to get closer to 70% this summer. We are getting close to the pre-pandemic timetable for accounts sign-off.

There are some problematic Departments. DHSC is one, because of the sheer scale of the issues it emerged from the pandemic with. Those are receding, so you will be pleased to hear that we are not qualifying the departmental group accounts on the PPE valuation this year, because it is no longer a material problem for those accounts. There is progress there. I do not expect DHSC to go from January to July in one leap, but we will certainly aim to advance it significantly for the coming year.

There are a couple of other Departments affected by the problems in local authority audit, where they have material figures in their accounts from local government pension schemes. The pension funds and their auditors have not been able to complete those accounts to allow us to sign off by the summer recess. We still do not think that they will by this summer either. DCMS and MOJ are the two affected by that, which is particularly annoying because in all other respects those accounts are ready to sign off in July. That is still a legacy of the problems in the local government audit market, which I know the PAC has taken a close interest in.

**Q24 Dame Meg Hillier:** I would love to talk about that now, but I think the Chair will lose his patience with me if I open up another channel. We have now gone through the supplementary estimate for the financial year. Do you expect to come back with any of this in future or are you now confident that you have bottomed out the issues we have been discussing?

**Gareth Davies:** I think they are exceptional. We have obviously talked about the machinery of government—

**Q25 Dame Meg Hillier:** They should be exceptional. I am just wondering if you can guarantee that you are confident in that?

**Gareth Davies:** Obviously, I cannot guarantee. The Commission will be quizzing me on audit quality at another session. The point about that is that it is non-negotiable. It certainly is not open to me to say, "Well, that's all the audit work I can do within my budget, so I'm going to go ahead and give the opinion anyway." I have to carry out the work in line with auditing standards—that is an absolute. I cannot rule it out, but we budget very carefully to make sure that this is not necessary, unless we get extreme circumstances like machinery of government changes or the intervention of IFRS 16. We do not think anything of the significance of those two events will affect the coming year.

**Q26 Dame Meg Hillier:** I would just caution that, with a general election coming and lots of political turmoil, are you factoring in things like machinery of government changes as a possible risk in your baseline planning, so you are not having to come back with a supplementary estimate?



**Gareth Davies:** We cannot make an estimate for that. You will see our estimate for next year soon actually, in March. We cannot make an estimate for the election, because clearly we do not know the timing or the result, let alone the detailed plans that might flow from its result. We will be presenting a budget for next year on our best available knowledge. Our long-standing practice, which the Treasury supports, is not to include contingencies for unknown events. The discussions at previous Commission meetings have been that it is actually preferable and more transparent to use, if necessary, the supplementary process—obviously, only when required—rather than pad our estimate in a way that might not be needed.

Q27 **Mrs Hodgson:** You plan to make a £1,500, non-consolidated payment to junior staff following updated guidance from the Cabinet Office. Does that apply to all junior staff, including those who may have just joined or are working their notice? Are any conditions applied to it? When do you plan to make the payment?

**Gareth Davies:** Again, this issue arose because the agreement for the civil service pay arrangements was reached after our estimate was agreed. To answer your question directly, we have some conditions. We have tried to replicate the conditions that apply to the civil service agreement. We are not bound by that, obviously, but we do try to match it where possible. The first thing is that we are paying this to all staff below our senior manager grade. To answer your question directly, that is everybody, including people in administrative roles as well as auditors and value-for-money specialists. That matches, I think, the way in which it was done in the civil service. Eligibility for this is also fixed at 31 October. Everybody who was in post at that point is going to be eligible for this payment, and we are pro rata-ing it if people are working on part-time arrangements. So those are the eligibility arrangements for it. I don't think, Daniel, there are any other conditions—

**Daniel Lambauer:** Only that they had to be in that grade on 31 October and have to be still working with us currently. If they have left between 31 October and once we pay this out, they will not get the payment.

Q28 **Mrs Hodgson:** When are they going to get this payment?

**Gareth Davies:** We are aiming to pay it in February, assuming the Commission approves it.

Q29 **Mrs Hodgson:** The National Audit Office justifies higher salaries than the civil service by saying that your main competitors for recruitment are private firms. Given that there are reports of slowing recruitment in the private sector, do you think that using the civil service awards as justification for a one-off payment to your staff is reasonable? I have a couple more questions on this, but I will let you answer that first.

**Gareth Davies:** This was a really important component in agreeing our pay framework changes, which we discussed at a previous Commission meeting. It was an important element in reaching a settlement with our



staff side on those new pay arrangements, and those arrangements are all geared up to address the challenge of retaining and recruiting the quality of staff we need to do a good job. The Commission will remember we hit some quite serious turnover problems a year and a half ago, so this whole pay change, the framework change, was designed to address that. It has involved restructuring the grades for newly qualified auditors to encourage retention, and so on. Our experience since then is that it has addressed the kind of crisis level that we were hitting a year and a half ago, but we are still tracking at around our target level of turnover for newly qualified auditors of around 20%. That is quite a high level of turnover. It isn't high in the context of newly qualified accountants. It's a very lively market, and as soon as our staff qualify, they are bombarded with LinkedIn offers from recruiters, and so on. So keeping it at 20% is actually quite hard work. We certainly haven't seen it dropping a long way below 20%. There is no let-up in the pressure from the external market, and it isn't just the private sector that we compete with. A lot of our staff leave to join the civil service, actually, or go into finance roles in Government, charities or other parts of the public sector. They go in all directions.

The figure that really matters to our effectiveness as an organisation is our vacancy rate and our turnover rate, and we manage very carefully to this 20% turnover level.

**Q30 Mrs Hodgson:** Do you consider this payment more a cost of living payment or a retention payment?

**Gareth Davies:** It was clearly driven by very high cost of living increases and inflation levels, for the year we're talking about, much higher than the pay levels we were able to agree. The same goes for the civil service. The context of this being agreed for the civil service was that it was a contribution to the undoubted financial pressure on staff in that year, and it is a one-off amount that is not consolidated into future pay levels, to recognise the exceptional level of cost inflation everyone was facing, particularly lower-paid staff, in that year. That is the origin of it. It was very important to our staff that it was replicated in their pay arrangements.

**Q31 Mrs Hodgson:** You have brought forward some aspects of the implementation of the new pay framework. Why is that?

**Gareth Davies:** Again, all this was about retention and recruitment. Having designed our new arrangements, particularly this new grade—essentially, once you qualify with us, you can move into an audit manager grade earlier than our previous arrangements allowed—that has been key in bringing retention up to the target level. We had designed this thing and we thought it was going to work well, so why would we take three years to implement something that we needed straightaway? I think that was one reason why it has been broadly successful in allowing us to plug our vacancies.

The other really important bit of data on this comes from our quarterly staff survey. There were two areas where staff were most concerned in



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our most recent surveys, which we have discussed in previous meetings of the Commission: one was pay and one was workload. The latest quarterly figures on pay have significantly improved since the implementation of our new pay framework, both for our audit staff and for our corporate services staff. That is another really positive indication because that feeds through into retention and staff satisfaction, and motivation and performance. Those are the key bits of data that we keep a close eye on.

**Q32 Mrs Hodgson:** One tiny last question. Do you have, just off the top of your head, the average length of service for people at the NAO?

**Gareth Davies:** No; I don't think we have that in front of us.

**Mrs Hodgson:** Under five years, five to 10, 10 or more and so on.

**Gareth Davies:** No. I could certainly get you that information by grade as well, because it does vary a lot by grade, but you can certainly build a long-term career at the NAO. That used to be very common—it is still quite common, because of the variety of the work and the chance to move around different roles in the structure. We also have this unique access to extremely interesting parts of the public sector that you can't get in other audit jobs. Many people find that quite addictive actually, and that becomes part of their career. But also we have people who have come to become a chartered accountant and want to see where else that can take them in their career. We welcome that as well because that kind of interchange in both directions is healthy for us as well as other parts. So there are people who leave soon after qualification and they occasionally come back to us, actually, later in their career. But I can certainly get you the data on length of service.

**Q33 Chair:** Do you have a higher turnover rate than generally within the civil service?

**Gareth Davies:** Yes, for those newly qualified accountancy grades. If you take the bits of finance departments that also have newly qualified accountants, I think you would see a similar level of turnover in the civil service, but compared to broad administrative grades and so on I think it is higher because these are very in-demand, qualified professionals.

**Q34 Chair:** I am interested that you say that it is not just the private sector that snaps up your newly qualified staff but also the civil service itself and charities. Is that because audit staff are particularly sought-after? Do you train them to a very high standard?

**Gareth Davies:** Yes. Also we are one of the largest training schemes in the public sector for qualified accountants. Actually, it has been very noticeable, following the loss of the Audit Commission, which had a similar-sized training scheme aimed at auditors in local government and the NHS, that the NAO really is the only large, public-sector-focused accountancy recruitment outside the civil service, and we recruit more trainees every year than the civil service, which does not organise a central scheme in quite the same way as we do. We need to have this scheme for our own purposes, but actually it would be a big blow to the

rest of the public sector if the NAO wasn't training 80 to 90 accountants every year.

Q35 **Chair:** Do you do an exit survey when people leave, to find out why they are leaving?

**Gareth Davies:** Yes.

**Chair:** And that is generally, what—career improvement?

**Gareth Davies:** Yes. It tracks our people survey data, which I mentioned earlier. Pay was a big issue for a while—about 18 months or two years ago. That has receded a little bit since we made our changes. The biggest single bit of feedback to us is on career development. In other words: "I want to do something that isn't audit," or, "I think I've reached as far as I am going to reach at the NAO and I can see an opportunity to progress faster somewhere else." Those are the most common examples we get.

Q36 **Dame Meg Hillier:** You recently lost a tenant in the London office. They used a break clause. What is the notice period for implementing the break clause?

**Daniel Lambauer:** I will need to get back to you on what it is exactly, but I think it is usually between three and six months.

**Dame Meg Hillier:** So you had some notice?

**Daniel Lambauer:** We had some notice of it, yes.

Q37 **Dame Meg Hillier:** That is the prerogative of a break clause.

You have been seeking a new tenant. Can you tell us who you have?

**Daniel Lambauer:** Yes. We have recently been quite successful at attracting new tenants. Three new tenants have signed up.

Q38 **Dame Meg Hillier:** And that is for that vacancy? They are all in the same space?

**Daniel Lambauer:** Yes. We have 12 floors in total. We have seven floors that we need to rent out, I believe. We have found five. We have three to go. Two, we are currently—

Q39 **Dame Meg Hillier:** This tenant was a big loss?

**Daniel Lambauer:** It was one of 12, so yes, it was. But we have been successful in getting one private sector tenant in. We have also forged better links with the Government Property Agency in relation to those Government bodies that ethical standards will allow us to rent out to, so we have two additional floors rented out to Government bodies or Government-related bodies.

There has been a good number of viewings and interest from private sector tenants, as well as from other public sector bodies and some charities. We have made some changes to the way we market the



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building. We have worked with our agents a little bit harder—let's put it like that.

We are also making some slight layout changes in the building. I know you know the building quite well, but one piece of feedback we had was that our reception area is probably a bit too NAO branded. We are going to rebrand it slightly, while still maintaining our brand, obviously.

Those small changes made a difference to our private sector tenants. We are hopeful, now that the market has settled a bit, that we are going to have more—

Q40 **Dame Meg Hillier:** Just to be clear and to recap, how much have you still got to let? What is the rough timeframe for that?

**Daniel Lambauer:** In terms of made-up floors, after these contracts are signed, we will next need to sign three more contracts if we are to have everything let out—we are aiming for two. We are keeping two floors vacant, because we are hoping to get your agreement to the refurbishment of the London office, and then we will need two floors onto which to decant our people. The net number is five, but two will be kept vacant for us to decant onto.

Q41 **Dame Meg Hillier:** You are confident that you will fill the space that you are trying to fill in the next very short period of time?

**Daniel Lambauer:** Yes.

Q42 **Dame Meg Hillier:** How have you managed conflicts of interest? You are working with the Government Property Agency, and bits of Government might want to move in with you. As you said, you access all areas, so it is sensitive work that you do. How do you manage that?

**Gareth Davies:** That is a really important question. Ethical standards are very clear on business relationships between auditors and the people that they audit, as you would expect. The first rule is that it cannot be material to either party. In practice, that means that they have to be a fairly large public sector organisation, and usually a part of them rents space in our building. We have turned down two offers from smaller public bodies, because it would have been material in their accounts. Ethical standards rule that out, so we are very clear about that.

It cannot be material to us, either. We could not rent out six floors to one public body, for example, because that would be material to our accounts. It tends to be that we can let one or two units to any one participant.

Q43 **Dame Meg Hillier:** That is the public sector?

**Gareth Davies:** Yes. That refers to people we audit. A good example is that one of our tenants is the NHS Providers organisation. That is not a public sector body we audit, but it is clearly very connected; it is a representative for NHS trusts and so on. That is a straightforward ethical decision for us, because we have nothing to do with their audit process, and they are an extremely good tenant.





As well as the decision on whether we can do it in principle, there are the practical safeguards that we put in place once our tenants are there. The people who deal with the rental contracts are not part of our audit teams; they are our facilities teams. And they only do commercial work for the NAO; they don't do any audit work. There is no contact between those teams, as part of that commercial relationship between the audit team and the audited body. We also have very clear guidelines for staff on confidentiality of information. Loud discussions in our foyer about sensitive audit matters don't happen because of the very clear understanding that public areas of our building are shared areas, and we have to maintain confidential information.

**Q44 Dame Meg Hillier:** What about the private sector? Having certain private sector providers might be inappropriate or there might be ethical issues.

**Gareth Davies:** We have a low-risk appetite for that. We have a clear process for assessing potential tenants and making sure that there would be no embarrassment or reputational risk to the NAO if they were our tenant. That includes whether they are going to pay us, of course—that is the other key thing. One of the advantages of public or quasi-public sector tenants is that we can be guaranteed payment, but our experience of that with private sector tenants has been very good.

**Q45 Dame Meg Hillier:** This unexpected break clause, although you had some notice, meant that you lost £0.8 million in revenue. You quite impressively found that by undergoing this rigorous budget review, but that rather begs the question, Mr Lambauer or Mr Davies, of why you could find that magically when you needed it and why you don't do that every year. Is there that money down the back of the sofa every year?

**Gareth Davies:** Every time we hit a budget pressure, and this is an example of an in-year budget pressure, our first job is to ask how we are going to accommodate that and live with it. We only want to come here when we really have tried everything else possible. A lot of this happens in-year in a way that we wouldn't normally trouble you with, but we thought that as part of the overall picture for this year, we ought to explain what has happened. It is largely reprioritising things that we did need to include in our budget but have decided to delay.

**Q46 Dame Meg Hillier:** That is particularly the training and IT initiatives that you delayed. Is that not just putting off the problem until next year?

**Daniel Lambauer:** As the C&AG explained, first, for the record, it is not just because of one break clause. We were hoping to have two additional floors rented out, which are signed contracts, and income for most of this financial year. However, the income is only starting at the end of the financial year because people are only moving in now.

**Q47 Dame Meg Hillier:** So there was a slight delay in implementing it.

**Daniel Lambauer:** That's right. The large part is to move expenditure to the quarters of the next financial year, so the actual operational impact is significant but not that significant. There are some areas that we are also looking into. For example, ideally, we would have liked to get some





external support in, but we can do it in-house. That is probably an opportunity cost because if you do a training in-house rather than with—and we don't do a lot of this—external providers, the training team can't do other things. As the Comptroller and Auditor General has said, it is £800,000 out of a £100 million budget. It is a very complex budget with lots of budget lines, and we usually manage just within. That does not mean that we have a contingency line at all in our budget—we don't—but we just have to prioritise throughout the year.

**Q48 Dame Meg Hillier:** So basically what you are saying is that that rescheduled training is just slipping from the end of the financial year to the beginning of the next, and because your rent will be coming in by then, it will all smooth out?

**Daniel Lambauer:** Right.

**Q49 Mrs Hodgson:** Can I just clarify something? You say that you are holding back two floors that you are not going to rent out in order to decant some staff from the northern office.

**Dame Meg Hillier:** The London office.

**Q50 Mrs Hodgson:** Right. Is that going to be temporary? You used to rent out 65% and it is going to drop to 40%. Is that because of the space that you have to rent out? Are you then hoping to go back up to 65%?

**Gareth Davies:** First, part of our response to our experience of the pandemic was to reduce the space that we occupy in our building in London, so the rentable amount is now significantly bigger than it was before. About 55% of the total space in the office is now available. We are aiming to rent that externally. Of course, once we achieve our full amount, that will reduce the cost of the NAO to the taxpayer. A big part of our efficiency drive is to use only the space that we absolutely need and rent out the rest. That is the background to this plan. When we bring our estimate for the new financial year—the 2024-25 year—to you, you will see that we are proposing to refurbish the London office, because it is 15 years since it was last touched and lots of things have worn out. Coming back to this hybrid way of working after the pandemic, we have learned that we need less space, but we also work in a different way, so we need different kinds of space, which we do not have at the moment. Instead of banks of hot desks, we need more collaborative space and so on. We have a successful design that we have used in the Newcastle office, and which we now want to replicate in London. That is the background to this change. We are proposing to do that over two years—2024-25 and 2025-26—and to do it in stages. As a floor in the London office is being refurbished, we will decant those staff into one of the empty floors we have talked about, which would otherwise be lettable—obviously, that is free to us, so it is not as if we have an extra cost—and then move people back in once the refurbishment is done.

**Q51 Mrs Hodgson:** But you would lose the rental income.

**Gareth Davies:** For two years. If we are able to complete the project in two years, we will rent out those two floors.



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**Q52 Chair:** You unexpectedly lost a tenant, so have you made a conscious decision to break that up and to have several tenants, rather than one large one? You will have a potential loss again when they leave en masse and you have a huge drop in your budget.

**Daniel Lambauer:** All our tenants occupy one floor. We basically lost one tenant from one floor, but we have now found another tenant for a similar-sized floor. It is not that we had one large tenant who we then lost; we just lost one tenant from one floor.

**Q53 Chair:** So it is not the entire space. Can I ask you about the capital funding for this year? You have delayed procurement of the equipment. Is the current equipment fit for purpose? You made a speech last week in which you identified this as being an area where other Departments were being deficient. They could improve their efficiency by upgrading their equipment and their software—a case of physician, heal thyself?

**Gareth Davies:** Absolutely. I have got my own words ringing in my ears as we talk about these issues. What I was describing there was having a credible asset management plan for the public estate and IT assets. The absence of that in some very important areas, like schools and so on is becoming very high profile and obvious. Here, though, we are talking about our desk-based monitors that allow people to use a bigger screen when they are in the office, and extending the useful life of those by one year. We want it to tie into the refurbishment programme that I have just described. It makes sense to do it together, because they will be part of the refurbishment process. The reason why we think we can get another year out of these monitors is that they were not as heavily used for a year and a half, during the peak period of the pandemic, as they would otherwise have been. With everybody working at home for months, those were not being used, so the wear and tear on the screens and so on is less than you would expect after the four years of their life so far. We think this is a balanced decision. We think we will get full use out of them and replace them when we do the upgrade to the office.

**Q54 Chair:** I have just got one other question, which is about the machinery of government. It is probably a question for another day, but what is your assessment of breaking up two Departments by creating three? Will the Commission be looking into whether this is an efficient form of government? Coming from local government many years ago, I can remember being advised that restructuring was a complete waste of money. Will you be coming out with an opinion on that?

**Gareth Davies:** Not from a policy perspective. It is absolutely for Government to decide what Departments it needs and so on—that is not for us—but how well managed that process is definitely is an issue for us, because it affects the use of resources and value for money. The NAO has looked at that general issue before. How well are these managed? Are there lessons to learn about doing that more efficiently? We need to accept that Governments will want to change the way the civil service is set up from time to time. How we do that to best effect is the question, so I think we will come back to that.



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**Chair:** Thank you very much for your attendance this morning.