

Public Accounts Committee

Oral evidence: NAO Main Estimate 2024-2025, HC 510

Monday 19 February 2024

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[Watch the meeting](#)

Members present: Dame Meg Hillier (Chair); Olivia Blake; Sir Geoffrey Clifton-Brown; Gareth Davies; Mr Jonathan Djanogly; Peter Grant; Ben Lake; Sarah Olney; Sarah Owen; Ms Marie Rimmer; Gary Sambrook.

Marius Gallaher, Alternate Treasury Officer of Accounts, HM Treasury, was in attendance.

Questions 1-35

Witnesses

[I](#): Gareth Davies, Comptroller and Auditor General, NAO, Daniel Lambauer, Executive Director (Operations), NAO, and Rebecca Sheeran, Executive Director, NAO.

Written evidence from witnesses:

– [Add names of witnesses and hyperlink to submissions]

Examination of witnesses

Witnesses: Gareth Davies, Daniel Lambauer and Rebecca Sheeran.

Q1 Chair: Welcome to the Public Accounts Committee on Monday 19 February 2024. Today, we will first examine the National Audit Office's main estimate for 2024-25, the next financial year. I will introduce the witnesses from the National Audit Office in a moment, but I am also delighted to welcome the Exchequer Secretary, Gareth Davies MP, who is officially a member of the Committee, symbolising the connection between this Committee and the Treasury in our joint desire to see public money spent wisely. I will leave viewers or aficionados of the Committee to decide how we each perform in that area. Minister, will you say a few words?

Gareth Davies: Chair, Committee, thank you very much for having me. I took great interest in the list of witnesses today—you wait all your life for a Gareth Davies to come along and you get two in one go. I have to say, I should have known this, but I thought that the NAO was the Naming Alignment Office, given the name of your witness today.

It is a great pleasure to be here. You do not need to hear this from me, but I will say it anyway: the PAC is one of the most prestigious and influential Committees in Parliament, challenging Government and public bodies on how they spend public money. That is something that at the Treasury we very much endorse and support fully, as well as the role of the Comptroller and Auditor General at the NAO.

I was quite struck by the statistic that 90% of the recommendations that are made by this Committee are taken forward and accepted by Government. I provide an assurance that the Government will continue to do everything they can to ensure that those accepted recommendations are delivered in the timeline stated when accepted.

I also recognise the great work of the Clerks and staff of the Committee in taking forward the work that you all do so well. Finally, as a member of the Committee, I tell you and provide assurance that I will continue to monitor your work, read your Reports and ensure that the relationship between the Treasury and this Committee will remain strong for many years.

Q2 Chair: Thank you very much indeed, Minister. I am delighted that you recognise the importance of Departments following up on our recommendations. That is something that we as a Committee monitor, and we call permanent secretaries back before the Committee if we feel that they have not followed through as they promised. I am glad that we are united on that issue. I know, Minister, that you have an awful lot of important work to do at the Treasury, so we understand that you may need to leave. We also thank you for your work in watching taxpayers' money.



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I now introduce our witnesses for the NAO main estimate inquiry: of course, we have the other Gareth Davies, the Comptroller and Auditor General and head of the National Audit Office; he is joined by Daniel Lambauer, who is an Executive Director at the National Audit Office, and by Rebecca Sheeran, also an Executive Director at the National Audit Office. Welcome to you all.

We are looking at what you would like Parliament to grant you in funds, so we want to ask questions about the strategy you have had and will have going forward, and about your expenditure. We know, Mr Davies, that over recent years there has been a challenge in both recruiting and retaining qualified staff. Will you give us an update on progress in the retention of newly qualified staff in particular?

Gareth Davies: Yes, of course. The picture of both recruitment and retention has improved since 2022. If you remember, we were having particular problems at that point in a very buoyant market for qualified accountants. Indeed, we had to take some emergency measures to strengthen our position in the employment market at that point.

Since then, we have restructured our pay and grading system—a huge amount of work by our HR team, working with the staff side on that—with the purpose of making it easier to retain high-quality staff on qualification. That is the key point at which they are very attractive to other employers, so we worked very hard on that. The early signs are that that change has been effective.

We are now seeing turnover levels at the newly qualified grade exactly on target, although that is still 20% a year. That is still a significant level of turnover, but it is a healthy level for us, because it means we retain 80% of the accountants we train, and then 20% go on to other jobs in the public or private sectors. Of course, that level of turnover allows us to recruit the next generation of auditors. So on retention, it is so far, so good.

On recruitment, we have a good indicator. Our biggest single recruitment exercise every year, as the Committee knows, is our graduate and school-leaver programme, and we are well into that programme for the intake who will join us this autumn. We have already filled 65 of our 100 or so vacancies for the autumn, which is good progress for February—that is where we would hope to be by now. We are working hard to fill the remaining slots by late spring or early summer. That is another indicator that we are broadly on track to have the resource we need.

Q3 **Chair:** When I went to visit the office in Newcastle, I met some of the school leavers, among others. I understand that you outsource the recruitment for graduate trainees.

Gareth Davies: We outsource the technical assessment programme, the software that is used for that and so on. It is administered by our own recruitment team, who do a great job in doing that. Our staff join the recruitment team at careers fairs at universities, and they do school visits



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for the school-leaver programme. So there is a lot of volunteer effort from our staff in carrying out that part of the process.

- Q4 **Chair:** Okay. In terms of costs, is it most cost-effective to outsource it, or have you been looking at insourcing?

Gareth Davies: The bit that we do outsource is, yes. It is an industry-standard programme that many other large employers use, so it would not be cost-effective for us to work up our own version of that. The part that depends on making good decisions about who to hire, whether they would fit the NAO's values and so on is done by NAO staff.

- Q5 **Chair:** And real people, not AI?

Gareth Davies: Absolutely.

- Q6 **Chair:** You have made assumptions in this estimate for what you will need next year, including a pay award of 3%. Given where inflation is, is 3% going to be enough? It is not that we are keen for you to spend more money necessarily, but we have talked about retention; will 3% mean that you can retain staff at all levels?

Gareth Davies: Our practice is to use the OBR's official estimate. Of course, we are talking here about April onwards—so the year from April '24—and 3% is the OBR's latest estimate of inflation for that period. In fact, if you listen to the forecasts at the moment—of course, we know that they are just forecasts—some forecasters are saying we will get to the target level of 2% inflation in the middle of the coming financial year, so it does not feel unrealistic as a working assumption. It is the best one we have at the moment.

I suppose the key change from a couple of years ago is that we are starting from the stronger position that I was describing. The external benchmark that we have been able to do recently shows that that change we made to our pay and grading, which I was describing earlier, has put us in a more competitive position than we were in two years ago. There is still no room for complacency, but it feels like we are in a better place.

- Q7 **Chair:** If there is a change in inflation—forecasts are forecasts, as you say—will you be coming back with a begging bowl to Parliament?

Gareth Davies: We will try not to. Parliament would prefer us to avoid supplementary estimates and so on, but on the—

- Q8 **Chair:** And so would the Public Accounts Committee.

Gareth Davies: Exactly. On the other hand, we have had a very clear steer from the Public Accounts Commission over the years: it would much prefer that we were transparent and efficient in our forecasting and that if, for whatever reason, it became necessary to ask for more resource, we did that separately, rather than pad each year's budget just in case. That has been our practice.

- Q9 **Chair:** In the accounts, non-staff costs are set to increase by over 10%, and one of the drivers of that is business support costs of £1.5 million.



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Can you explain that figure and whether that is the driver for the additional 10%?

Gareth Davies: The biggest driver of non-staff cost increases for next year is inflation. We have seen particularly significant price rises from the work we externalise to the firms. That includes the number of audits that we outsource to the firms because specialist skillsets are required and so on. I could say more about that, because an element of our plans is to look at that proportion of outsourcing for the next few years. That is one big driver.

We also use the firms for specialist technical advice, and again the rates there have gone up considerably more than the headline inflation rate, so we are seeing significant cost pressure too. On business support, I will ask Daniel to talk about where some of the other cost increases are.

Daniel Lambauer: Inflation is one part of it. The other part is what I would call demand-driven increases. For example, we have more auditors in the business. That means more software licences for some of the key software. The more data we use, the more data storage we have. So there are some increases in our digital functions. There is also some increase in relation to investment in cyber-security that we need to make in the current environment. There is also some small investment in our HR team, to better support the training experience and fund welfare initiatives we want to introduce and occupational health assessment. Most of the increase is demand-driven; the vast majority in this context is because of inflation.

Q10 **Chair:** Is any of it because of rescheduled costs from last year, or did you absorb that into the budget?

Daniel Lambauer: Most of the rescheduled costs from last year are in another line, which is the audit technology line. We wanted to do some pilots on emerging technologies last year and we then moved that to this year, partly to give us a bit more time to really assess whether it is worth while investing in them.

Q11 **Mr Djanogly:** Good afternoon. As with any professional services organisation, the cost is in people, and your overall staff numbers have increased substantially. In 2024-25, you will employ over 1,000 people—1,010 people—compared with 863 at the start of your strategy period four years ago. What accounts for such a rapid expansion?

Gareth Davies: Growth in the volume of the audit work, essentially. Of the four main drivers of that growth, the biggest one is the fundamental change in regulation of accounts and audit over that period. We have seen the regulatory response to the problems of poor-quality audits and so on from a few years ago. That is now biting very hard. In every sector, audit fees have increased significantly, to reflect larger volumes of audit work made necessary by new auditing standards. For example, for anything in a set of accounts that requires valuations by professional valuers or that requires modelling and estimates—in other words, a figure that has a lot of judgment in it—the level of audit challenge and expert advice that goes



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into each year's audit of those numbers is completely different from a few years ago. Significantly more audit work, driven by changes in auditing standards, is the No. 1 reason.

We have taken on significantly more audits in that time as well. In the year that we are looking ahead to—next year—we are taking on another 2% increase in the number of audits we do, and some very significant ones, like a whole new Government Department after the machinery of government changes. We are also auditing for the first time the companies that form Sellafield, Magnox and so on as part of the NDA group. We have always audited the NDA itself, but not its subsidiaries. Quite tellingly, those subsidiaries have been unable to find a private sector auditor. When their contracts came up for retender, nobody was prepared to do their audit at what those companies regarded as anything like a reasonable rate, or in fact any rate at all. That is, again, a worrying indication of capacity in the wider audit market. In this case, we think there is a public interest in the NAO picking up those audits, because it will make our audit of the NDA group more efficient overall. We will get better assurance on the very large liabilities that the Committee knows sit within that group of audits. But that is an indication of the pressures on capacity in the audit market. So new audits are the second reason.

The third reason is that we are still bringing the timetable forward from the impact of the pandemic. It is taking several years to restore the pre-pandemic timetable. Last year we brought another 7% of audits back before the summer recess. We are aiming for a similar increase this year and next year. Of course, every time we do that, we are doing more than a year's work in 12 months, because we are bringing audits forward. That is another reason why that takes more resource.

The final reason is something I touched on in an earlier answer. We have looked very hard at the value for money of outsourcing audit work at the NAO. It is a long-standing practice, for good reasons. It helps us with capacity at the peak period. Crucially, it gives us access to specialist expertise where particular audits require it. However, the trend in the prices that we have been receiving from the firms to do that work has been sharply upwards—for the same sort of reasons as I was explaining for increases in all audit fees—but so much so that we have carried out a value for money review. At what point can we justify outsourcing this work in the way we are now? Is there an argument for bringing at least a proportion of that back in-house?

We think there is, so we are taking on some extra staff this year as part of a programme to be ready to take increasing numbers of audits in-house over the next few years. We will still outsource a fairly significant proportion. At the moment, it is about 20% of our audits. We expect to be in the teens once we have completed this programme. We think that just that change in the level of outsourcing will save the taxpayer about £1.5 million in cash—it is cheaper to have our staff doing that work than to outsource it by about that level. It may not always be so, so we will keep that under review and change the balance again in the future, if



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necessary, but it felt as though we ought to take our own medicine. We often recommend that Government Departments scrutinise their procurement and make sure that it is the best available value for money, so we are taking our own medicine.

- Q12 **Mr Djanogly:** Thank you for that comprehensive list. You mentioned the higher auditing standards and getting back on track after the pandemic. How can we, or the taxpayer, get an idea of the actual impact of those two items? You said there is an impact, but what is the impact of higher standards on your costs?

Gareth Davies: On the standards point—

- Q13 **Mr Djanogly:** Is it in some document—have I missed it?

Gareth Davies: As a qualified auditor, I have no option but to comply with auditing standards. As those standards have gone up, our audits have to respond. As the Committee knows, we are inspected on the quality of those audits. We have had some quite challenging feedback in recent years from the Financial Reporting Council, requiring a response. The unsatisfactory answer to your question is that there should be less of that challenging feedback from the regulator.

- Q14 **Mr Djanogly:** You say the impact of covid has been significant. How do we know what that significance is?

Gareth Davies: For example, the proportion of audits that we certified by the summer recess, which is our main target for the big Departments, fell from 78% before the pandemic to 41% the year that it first hit, and we have been gradually clawing back from there. We are now at 60%, so we are getting closer. That gives you an illustration. It is our firm view that good assurance is timely assurance—the later the audited accounts are available, the later Parliament can properly scrutinise what is happening in those accounts, and so on. Timeliness is a really important component of good-quality accounts, so we are very focused on getting back to the pre-pandemic timetable. That one is easy to quantify.

It is a bit harder to quantify the benefits of higher-quality auditing, although it is probably good to mention that a big part of the investment we have been making in the last few years is in our audit transformation programme. This year, that has culminated in us rolling out our new audit software platform for the first time. That will produce visible benefits for the Departments and organisations we are auditing and their audit committees, and for Parliament in scrutinising them, because it will not just make the audit better quality in a technical sense, it will give us more insight into what is going on in the finances of those organisations because we are using data analytics—more powerful analysis of spending patterns, and so on. So we will start to see significant benefits from that investment there.

- Q15 **Mr Djanogly:** You say you are recruiting more VFM staff to enable financial auditors to focus on their core work while ensuring that you “can provide wider support to Parliament...in the most cost-effective way”. Are



we going to get more support?

Gareth Davies: Behind that is the fact that traditionally, quite a lot of our parliamentary support was divided between our financial audit staff and our value for money staff. The pressure on the resources for financial audits mean that is less possible now. We are just recognising that, and rather than insisting on higher and higher workloads for the same number of VFM staff, we are boosting the capacity to be able to give Parliament the support it needs. There is always unmet demand in Parliament in terms of Select Committee interest in work from the NAO and briefings on particular topics for Committee members beyond the PAC. We have done a pretty good job in meeting that level of interest and demand in recent years. But it was right to respond to the feedback we were getting from our VFM staff, that they were finding that the workload pressures were not just intense, but becoming overwhelming. We needed to add some resilience into that team.

Q16 **Mr Djanogly:** As we head towards the world of specialisation and VFM staff are getting more and more distinct from audit staff, can you explain your thinking on having more auditors? Will you be bringing in more specialists eventually as well? Otherwise, you will have a mismatch.

Gareth Davies: It is the way that the work is going. We say in the document that this is the fifth and final year of our five-year strategy period. One of the biggest impacts of that strategy has been our specialist expertise hubs. For example, commercial procurement is one of our hubs, and digital is another one. These are topics where we must recruit specialist experts if we are going to be credible in our reporting on them. I think the Committee has seen the difference that that has made in our work on digital—for example, in risk management, where the Committee has been able to use our work to get to much more focused and specialist areas of what Government are doing on those topics. That has been broadly a success. We do not see that this is about huge additional volumes of those people. However, we definitely need to ensure that we are not dependent on one key person in those areas, so we have succession planning and capacity building in each of those hubs to ensure that when people move on, we have high-quality experts to replace them.

Q17 **Mr Djanogly:** As I recall, you are 80% auditors, aren't you?

Gareth Davies: Well, 80% of our staff are either financial audit or VFM, with the other 20% in support roles, but the split between financial audit and VFM is about two thirds financial audit and one third VFM.

Rebecca Sheeran: Our value for money teams, which produce the Reports for you, are typically blended teams. They will be a mixture of qualified accountants, auditors and those who have joined us through other routes. Our entry grade for the value for money service line is the analyst role. The additional headcount that you mentioned—the 12 people we are looking to bring in this year—will be largely at that grade, and we will train them up as performance auditors in the NAO. We expect all those who work on our value for money reports to look to deepen their expertise in one of our hub insight areas that the C&AG referred to. One of our



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areas of increased focus and investment over the year ahead will be learning and development and the skills pathway for those value for money auditors to develop specialisms in areas such as digital transformation, major programme delivery or commercial expertise.

- Q18 **Mr Djanogly:** Am I right that you are saying that even though things are becoming more specialist, it is still more cost-efficient to train your own people, rather than to use outside consultants? Would that not have been the case? Would that always have been the case, or has that changed?

Gareth Davies: It is certainly more cost-efficient to use our own people than to use outside consultants, yes. However, we take on to our payroll people with genuine market expertise in particular areas. That has been—

- Q19 **Mr Djanogly:** But nothing like we saw with the GAO in America.

Gareth Davies: I am not sure what you saw there.

Mr Djanogly: We saw a much higher use of internal specialists, rather than auditors.

Gareth Davies: Obviously that is in a much bigger-scale organisation, which is roughly six times the size of the NAO. Some things become possible at that scale that are not at our scale. In the areas that are crucial to value for money in government, we have been able to get really high levels of expertise both developed through experience with us and coming in from outside. For example, just this week was the start date for a director who has joined us to lead our work on regulation. As the Committee knows, we do a lot of work on the effectiveness of regulation in Government and the impact of that on value for money. We have somebody with a lot of external expertise in regulation coming in to head up that part of our work. That is a good example of the kind of thing we are able to do.

- Q20 **Sir Geoffrey Clifton-Brown:** C&AG, on the back of Mr Djanogly's questions about employing more specialists, does that give you more scope to try to procure more outside work? Should you expect therefore to increase your income?

Gareth Davies: In other words, fee-generated income from audit work—

Sir Geoffrey Clifton-Brown: Not just necessarily audit work.

Gareth Davies: Sticking to our knitting is our watchword. It would be very easy, because the NAO is regarded well internationally, for example, to do a lot of international work. We are clear that while international work is important to help us to understand what is going on around the world and help us innovate and challenge our current practice, we have to control the volume of it very strictly so that it does not become an unnecessarily large distraction from our core business, which is supporting the UK Parliament.

Sir Geoffrey Clifton-Brown: The tail doesn't wag the dog.



Gareth Davies: We are always very challenging. We certainly consider opportunities to do work outside our core areas, but it has to meet a high threshold. What value that will add to our core business of supporting the UK Parliament and making sure that the Government get value for money is always the test that we apply. Do we consider opportunities to do that? Absolutely. We have to watch audit independence, of course. If any of the work is funded by Government directly or indirectly, that can only be at a very de minimis level because we have to be independent of Government and therefore not taking its money.

- Q21 **Sir Geoffrey Clifton-Brown:** Mr Djanogly referred to our visit to the GAO. What more synergies could you achieve between the GAO, which does largely similar work to yourselves, and the NAO? I am thinking particularly about more international comparisons in your VFM reports. I am also thinking about the secondment of people. We learned that CAAS, the defence costing organisation, had a secondee in the GAO for 20 years. As a result, CAAS's handling of defence equipment costs and procurement has got much better than it was. Is there more co-operation that you could do with the GAO?

Gareth Davies: We certainly collaborate a lot. For example, we have recently been exchanging good practice on digital work. That is a live example. We do international secondments also. I think the GAO secondments you describe are in the US with the US Government, or parts of it. There are regulatory restrictions on secondments between auditor and audited body that are very strictly applied in the UK. Because this is a big issue for us, we have recently made welcome progress with the FRC on what we think is a more realistic version of that policy on secondments, so it will be possible for us to reinvigorate our programme of secondments to parts of government, subject to safeguards, of course.

Clearly, we must not second anybody to an area that they will subsequently audit, but you are right that there is a lot of value to be gained from them. We have had some very successful ones with New Zealand recently and their audit office. We are also in conversation with the South African audit office for secondments there. So we are definitely looking at those opportunities. As you say, with the US, where there are lots of similarities on the challenges we face, there are some particularly interesting opportunities.

- Q22 **Sir Geoffrey Clifton-Brown:** These two questions are probably linked. Looking at your purchase of professional services of around £16 million—this is in figure 4 on page 159 of the annual accounts—is that the figure that you have in scope for reducing by £1.5 million? How does that relate to your purchase of new data analytics and new audit software? You are making efficiencies on the way you do the audits, but you are taking on more auditors. How do the two square?

Gareth Davies: Even if we were changing nothing on the amount of outsourcing, we still need to invest in the data analytics because that is the future of auditing. People have been talking about it for many years. It is finally actually changing. The tools are now available that make it



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possible to download all the data supporting the accounts for a large organisation and use data analytics to analyse the entire population of transactions, whereas audit practice in the past was about sample testing. That is moving now. There are lots of conditions for that: we need a well-controlled IT system, of course, and we need to be able to guarantee the security of any data that we download. A lot of technical effort is going into making that a safe process.

Once it is working, the efficiency opportunities are significant for data analytics. The application of artificial intelligence to audit work is a rapidly developing field. I am pretty confident that at the end of our next five-year strategy, which will be at the end of my term of office, our audits will look radically different to the way that they look now, with this change that is working through. The new audit software we have just installed is capable of taking in new data-analytic tools as they become available. It is a very flexible system, so we are in a good position to realise the benefits.

I think that is all independent of how much we outsource to the firms. The reason that we want to bring some of that work back in-house, and therefore have more of our own staff, is that it is becoming prohibitively expensive to use the firms for certain types of audits. It still makes sense to use them for specialist-expertise areas, where it would be very expensive for us to have a small amount of highly specialised expertise, but it does not make sense for us to outsource the more straightforward audits to the firms. They are becoming more expensive. That is where, by taking on a few extra people ourselves, we will save that cash figure that I mentioned.

Q23 Sir Geoffrey Clifton-Brown: This is my last question before the Chair gets itchy feet over the time. Is this taking on of extra auditors a relatively short-term measure because, in the long run, you will get to a stage where you will only need a steady state of auditors?

Gareth Davies: That is potentially true if the data-analytics change that I mentioned drives significant reductions in the volume of audit work required. I think what we are expecting is that it will change our skill mix, as well as maybe the overall number of staff that we need. For example, we will need more data scientists, and that will become a routine part of our annual intake in a way that it has not been up to now. There will be a changing skill mix to recognise that this work is changing, and hopefully a volume reduction as well. Of course, that will depend on other things happening, such as how many audits we are asked to do and so on, but yes.

Q24 Ben Lake: Good afternoon. I should like to ask about your capital expenditure, if I may. I note that in last year's main estimate a proposed capital expenditure for the forthcoming financial year was set at £3.7 million, yet in this year's main estimate that now has increased by some 16% to £4.3 million. I am interested to know what the reasons are for that increase.



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Gareth Davies: Of course. The biggest single reason is that our periodic refurbishment of our office has come around. It has been 15 years since our London office was last refurbished, so quite a lot needs replacing anyway—carpets and decoration and so on—but we are taking the opportunity to also reshape the office. That is because we are sweating our assets more vigorously. We have reduced our floor space in the London office and we are letting out more of that building. The market is finally picking up for that, so we are increasing our rental income in the coming year quite significantly.

And, as we said, the organisation is still growing, so we are squeezing more people into a smaller space, and we are doing that by making sure that the space is suitable for the way in which we are now working, with more hybrid working, with people spending some time on client sites, at home and in the office in a typical week. The office is not really set up for that at the moment: it is just hot desks, whereas people want to work in teams when they are in the office. That is the reason for coming together—to work collaboratively—so we are creating more spaces for collaboration.

If you put all that together, it makes sense to do that work at the same time as our planned refurbishment. We will be moving people out into one of the empty floors, refurbishing their floor, moving them back in again, and working our way through the building in that way.

Q25 **Ben Lake:** So that I understand correctly, is the work to reconfigure some of the office to better suit the business needs something that has changed since last year, or is it just that the refurbishment costs have gone up?

Gareth Davies: The coming year is year one of a two-year programme, so we were not doing that work last year, but it is coming this year and next.

Q26 **Chair:** I should say that I wear two hats, as I am also on the Public Accounts Commission. We have looked a bit at your office refurbishment there, so I will have to remember where I have asked the questions before. You have had problems renting the office space up until now, and had a tenant who withdrew. Your plans do rely on renting that—it is obviously important income for you—and you obviously have the refurbishment, which takes certain floors out of commission. Can you explain how you are managing those assets? Mr Lambauer, I think you would be the best person to explain. We have heard a bit from the C&AG, but could you expand on that, because it is still a worry? The office market may be getting stronger, but it is still weak.

Daniel Lambauer: We have had some encouraging signs in the last half of this financial year just ending. As you will see in the accounts, we are now projecting £2.6 million income from the floors to be rented out, up from £1.4 million this year. That is because we added three new tenants at the very end of last year. As a result, to hit our financial target next year we need only to find two additional tenants for two more floors for



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the next financial year, which leaves us one more floor to fill; then we will have all the floors filled apart from the two we are using for decant space.

We had good interest in the floors that are currently available. I think an organisation came in multiple times to look at one particular floor, even bringing fitters along. That does not mean it is a done deal—we have been there before. We have made changes in our agents and refurbished our reception after feedback from one of the private sector tenants, and our work with the Government Property Agency has led to more interest.

Q27 Chair: Have you had any Government clients interested in taking space?

Daniel Lambauer: Yes. There are clear rules, as we explained to the Public Accounts Commission, about who we can take on in terms of materiality, but we have had subsections of larger Departments that are taking on space.

Q28 Chair: Could you explain the materiality point, Mr Davies? People might not follow.

Gareth Davies: We can enter into a business relationship with those we audit—for example, being their landlord—only if it is immaterial to both parties. In practice, that means we do not let out more than one floor to any public body, because that is immaterial to us; and it can only be a small part of a larger organisation, because if the whole organisation was occupying the floor, it would clearly be material to that party. That is a strict test, which we apply, and on those criteria we have had to turn down some keen tenants offered by the Government Property Agency.

Chair: It is worth rehearsing that it is a little more complicated for you than for similar landlords.

Q29 Sir Geoffrey Clifton-Brown: C&AG, may I come back to the whole business of late accounts, particularly in the local authority sector? It does affect your work, doesn't it? Because you need to gather pensions and other information for the whole of Government accounts. What effect is all that having on your business, and how many years do you expect that to last?

Gareth Davies: It is affecting our audits of central Government in two ways. The direct way is that two big Departments have material entries in their accounts arising from local government pension schemes because of historical transfers of staff from local authority functions to those Departments. The Departments in question are the Ministry of Justice and the Department for Culture, Media and Sport. Even though both are actually in a position where we could sign their accounts for all other purposes by the summer recess, we cannot do so because we are waiting for the audit of the relevant local pension schemes to be completed by those auditors. That is very frustrating for us and for the Departments.

The second way it affects us is in the whole of Government accounts, where local authority accounts are brought into all of the public sector accounts. The Committee will be aware that we had to qualify the most recent set of whole of Government accounts because of large gaps in local



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government accountability. Essentially, there were no audited accounts for a large number of councils because of delays in that sector.

Those are the two ways in which the accountability that you see here has been affected by that process. The Government are consulting on a new system of statutory backstop dates for local government audit. That consultation is live at the moment. We have worked collaboratively with the Department and the FRC on that, but it will not be a quick fix. It will take a little while to restore the timeliness of the local government system to where it used to be, when by the end of September each year, after the year end, essentially all local government accounts were complete. It will take some time to get back to that position.

Q30 Sir Geoffrey Clifton-Brown: It seems to me that one of the most important bits of work you do in a set of annual accounts for a Department is the assurance work; it isn't just the auditing of the numbers. Is there a bigger role for your office in assurance work? You are such an exemplar of methods of auditing, digital, net zero, safety and so on. It seems to me that you are a very good exemplar for a range of areas that you could offer to Government Departments and charge them for. Have you thought about that?

Gareth Davies: First of all, it depends on whether it is in our sphere of competence. Some of those are specialist areas that we would have to gear up to do separately, and at the moment that would feel like a distraction from our core business, which we have talked a lot about today. For example, we are not qualified to inspect on health and safety; those are specialist functions that others do.

There are some areas that are coming whether we like it or not, including sustainability reporting and audit assurance, on which there is a rapidly developing field of standards being set. We expect to be involved in the auditing of sustainability assertions in Government accounts. It is important that the Government demonstrates that it can live up to the standards it is setting for the private sector in those areas. We are already in the early stages of planning what that means for us, in terms of skills, knowledge and the capacity to do that at scale when it is required. It is not yet clear what the timetable is for that, but we are getting ready because we can see it is coming. That is probably the most tangible example.

Digital is a really interesting one. Again, there are people doing work on this. For example, the National Cyber Security Centre does a lot of certification of sensitive Government systems on cyber-security, and we would not want to trespass into that territory, but more routine audits of cyber-security absolutely fit within our area. We are looking at how we might gear up to make sure we can give the assurance we are already required to give on cyber-security, fraud prevention and detection and so on.

Q31 Ben Lake: Mr Davies, you mentioned the significant investment you are having to make to meet enhanced regulatory standards and more



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complex audit standards. How confident are you that the investment you outlined will be sufficient to meet these new standards?

Gareth Davies: I think we have made the right calls, actually. It is thanks to Parliament funding those investments, particularly in our audit transformation programme, that we have been able to do that. We have a brand-new audit methodology that we are applying for the second time and a new software package that we are applying for the first time. We could not have done that without Parliament giving us the resources to invest in those areas. I am very proud that the audit software, which is a huge development over three years, has come in on time and on budget. We are now putting it through its paces for real on every audit this year, so the proof of the pudding will be in the results of those audits and the inspections of those audits that the FRC will carry out.

Despite the inevitable teething trouble of implementing a new system for the first time—learning how it works, ironing out the initial bugs and so on—the feedback from the teams is that this is already a much more modern approach that is saving time in repeated inputs that are no longer required, and that is before we get to the really advanced data analytics that I was describing earlier. I am absolutely confident that it was necessary; we would really be regretting it if we had not made those investments.

Of course, we always say to Departments that they must realise the benefits of their big programmes, and that applies to us too. We are now completely focused on showing that this delivers better-quality audits, better insight for Government and Parliament and greater efficiency.

Q32 **Ben Lake:** It is good to hear that something is running on time and on budget. You just mentioned some of the benefits of the ATP; when do you expect us to fully realise and see those benefits?

Gareth Davies: I think it is going to be continuous, actually. As I said, the great thing about this is that it is not like software used to be: we are not implementing a new software package that we will have to uninstall in order to install a new one in a few years' time. This is a cloud-based software platform, and you just plug in improvements as they become available, so it is future-proofed. Once we have tested a particular thing—we are testing quite a lot at the moment—and it has proved itself useful, we will train everybody in that and plug it into the system, and it will be available, so this will grow over time. I would like to be able to come back here in a year's time to explain how the first-year implementation went and how the benefits have materialised. It is probably going to be a few years before we can say, "This is a completely transformed audit with greater insight," in the way I described earlier.

Ben Lake: Thank you very much.

Q33 **Mr Djanogly:** On the outsourcing of audit work, I note that in your accounts you say: "In 2022-23 and 2023-24, the cost of using external audit firms to carry out some of our audits and to provide specialist advice increased by an average of nearly 9% each year." How does that



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compare with the increases you are seeing? What is the difference?

Gareth Davies: It is higher. On volume like for like, we are seeing an increase of about 4% in our costs, so that is the gap that we are worried about. That is what has prompted the review that I was describing earlier.

Q34 **Mr Djanogly:** So we are looking for this transition in-house. What sort of time period are you talking about, and how much do we expect to save from it?

Gareth Davies: We have framework contracts that—if we use our extensions—run for another three years. Essentially, it is about getting ready for taking in audits in three years' time. We will be able to do that, and there are some opportunities earlier than which we will be taking, so it is a staged process. But we are looking to take in about 20% of the contracts by value that we currently outsource, so there will still be 80% of that work outsourced, but the other 20% we will take in-house. As I said earlier, we are looking to save between a million and a million and a half in cash by making that change.

Q35 **Mr Djanogly:** When you manage this process, it will presumably cause some element of disruption. Is that something that will in itself take resource?

Gareth Davies: No, actually, I don't think so. We are very used to changing the audits that we insource and outsource, and those audited bodies are used to those changes. Actually, at the moment, we are getting quite a lot of demand for bringing those audits back in-house from those audited bodies, so I think they will be willing participants, in most cases, in that change. Also, it will help us with bringing forward the work, and with that element of our agenda as well, so there are quite a few reasons why this will be well received. Our staff and the firms' teams are well used to managing the handover of audits, so I would not expect disruption.

Chair: I thank our witnesses. We will be writing to the Public Accounts Commission with our view about whether we should recommend your estimate or not. Of course, under the system it is the Public Accounts Commission that will agree finally whether or not to grant the money that you are requesting, so there is a little bit of time to wait. In the meantime, thank you very much indeed.