

Public Accounts Commission

Oral evidence: [National Audit Office Strategy and Main Estimate 2024-25](#)

Wednesday 6 March 2024

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Members present: Mr Richard Bacon (Chair); Jack Brereton; Clive Efford; Peter Grant; Dame Meg Hillier.

Questions 1-47

Witnesses

I: Dame Fiona Reynolds DBE, Chair, The National Audit Office, Gareth Davies, Comptroller and Auditor General, The National Audit Office, and Daniel Lambauer, Executive Leader, Strategy and Operations, The National Audit Office.

Examination of witnesses

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

Chair: Welcome to this meeting of the Public Accounts Commission on Wednesday 6 March 2024. We are joined by the team from the National Audit Office. May I ask the witnesses to introduce themselves?

Gareth Davies: Good morning. I am Gareth Davies, Comptroller and Auditor General.

Dame Fiona Reynolds: I am Fiona Reynolds, chair of the board of the NAO.

Daniel Lambauer: I am Daniel Lambauer, one of the executive directors of the NAO.

Chair: Thank you very much indeed. Peter Grant will start the questions.

Peter Grant: Thank you, Chair. For the record, I confirm that I am still a qualified member of CIPFA, which is involved in setting regulatory standards and similar work. Because a number of NAO employees will be CIPFA members, I will not be taking part in questions on related matters.

Chair: Noted.

Q1 **Peter Grant:** Mr Davies, you have reported that you continue to make significant investments in improving the NAO's capability to meet enhanced regulatory standards and to deal with more and more complex audit standards. How confident are you that the level of investment that you are putting in is sufficient to meet those challenges?

Gareth Davies: That is one of the biggest questions that we have had to consider in putting together our estimates over the last few years. As the Commission is aware, accounting and auditing standards have been radically strengthened since the scandals of the previous decade. That has had a significant impact on the nature of the audit work that we are carrying out, the volume of that work, and its cost. As you say, that is reflected here.

The first main investment that we have had to make has been in staffing. That includes training those staff in developing standards and then deploying them in sufficient numbers to cover the work required.

The second major area is one that the Commission is aware of: over the past three or four years, we have had our audit transformation programme, which has meant a big investment in a new audit methodology that we are now in the second year of implementing, and in what is now a brand-new audit software platform called APEX. The Commission has approved the investment necessary to develop both those strands of our new approach, and we are now into realising the benefits of those investments.



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Those are the biggest areas. The final thing to mention under this heading is the substantially increased cost of our use of the expertise of the private firms. One of the consequences of higher standards is greater use of expertise outside the audit team where required—on valuations, estimates and so on. Not only are we doing more of that, but the cost has gone up quite steeply in line with costs in the wider private audit market. Those are the main investment headings.

Q2 Peter Grant: Do you still expect to finalise the implementation of the audit transformation programme in 2024-25?

Gareth Davies: Yes. The big investment in the new methodology and the system that I described will be complete by then. The software platform itself is designed to have a long lifecycle of at least 15 years.

The big advantage of this approach is that the days of implementing a software package that becomes obsolete, requiring you to install a new one, are gone. Software is essentially a service now; all our data is held on the cloud and we can plug in improvements to elements of the system as they become available. We will be continually upgrading this, which will be business as usual over the next few years, but the major investment programme will be complete on time.

Q3 Peter Grant: As you know, we will be looking at audit quality in more detail later in the year, but for now, the report from the Financial Reporting Council raises some quite significant concerns. What would you say to those who say that you are asking for money to invest in improving audit quality, but there are some indications from other professionals that the audit quality is, if anything, going backwards? How would you answer that?

Gareth Davies: I agree that the report we have had from the FRC shows that we have further improvements to make. We are very much in the “holding our nerve” phase of this programme of investments, because we have been doing the right things to improve audit quality. None of the audits using the new methodology or the new software platform that I mentioned has yet been inspected as part of the quality review process. I am very confident that they are making a positive difference.

Because we are later than usual in the cycle on the report that you mentioned, the latest round of FRC inspections is well under way now. It is obviously too early to comment on the results, but I would expect the improvements we have been making to come through much more clearly in the results. But you are right that the report shows that we absolutely still have improvements to make.

Q4 Peter Grant: When you gave evidence to the Public Accounts Committee—I am sorry that I was not able to join you for that session—you said that the audit transformation programme was facing “teething issues”. Could you give us more detail on what those teething issues have been?



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Gareth Davies: Yes. Overall, the programme is in very good shape. The software was released to the organisation on time and on budget, which was a big achievement for the team involved. We had an industry-standard programme of testing and piloting before that roll-out. As with anything, once it hits several hundred people using the system all at once, you learn things about capacity, the speed of response and bits of functionality as well. We have had a very good programme of work with Tisski, our technology partner on this project, responding very quickly to those issues as they are identified by teams. Anything that has been raised so far we have been able to fix very quickly, so there has been no substantial impact on the delivery of the audits.

Q5 **Peter Grant:** Does “no substantial impact on the delivery” mean that these teething issues are having a significant impact on the quality of audits over the past year or so?

Gareth Davies: No. They are all about ironing out the way the system works in practice. The system itself will help us to deliver quality much more reliably, because essentially it provides much stronger guardrails for audit teams, making it much easier to do the right thing the first time. The way the system works makes it much more difficult not to do the right thing. None of the bugs that needed fixing compromises those strengths of the new system.

Q6 **Clive Efford:** It appears that the recruitment and retention problems that you have faced previously are now less acute. How confident are you that the 3% pay increase will not undermine your recruitment and retention and lead to you returning for another estimate?

Gareth Davies: Maybe I could bring Fiona in, because the board and the remuneration committee have been taking a close interest.

The way I would characterise the situation at the moment is that we have stabilised the position on retention and recruitment. We are now at about our target level for retention, which is a good thing, but we are absolutely not complacent. There remains a good, strong market for qualified accountants, so the onus is on us to make the NAO an attractive place to stay and develop your career. That is where a lot of our focus is going at the moment.

Sorting out the pay framework in the past couple of years has been a big component of our retention plans. All the benchmarking evidence we have tells us that we are now in a more competitive place than we were, as a result of implementing that new pay framework, but we are absolutely staying focused on what the data is telling us about retention and recruitment.

A very good indicator is that our graduate recruitment programme for the coming year is on track. We are aiming to recruit a significantly increased number this year: about 100, compared with the normal figure of 80. We have already accepted offers in the mid-70s, which is ahead of where we had expected to be at this stage in the year. Those indicators are telling us that we are about right.



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Your question also touched on the pay award for 2024-25. Our normal practice, which we have applied again, is to use the OBR's latest published estimate of inflation for that year, which is 3%—that is the best available at the time. We have to come to you to seek approval for our estimate. As far as anyone can tell from the forecasts that are available, that feels like a robust place to be at the moment. It is fair and responsible, given that this is public money, but it is also realistic about what it will take to retain our people.

Dame Fiona Reynolds: Using the broad OBR guidelines is what we are supposed to do. We also feel that that is a reasonable place to be.

I also emphasise our focus on the non-remunerative aspects of working for the NAO. Everything we do, from making sure that the office spaces are a good place to work to looking at how we plan and resource the work of our staff, has a big impact on retention alongside levels of pay. We think we have made a big step forward on levels of pay, but we are looking to ensure that we provide an attractive place to work as one of the reasons why people would stay.

From watching the private firms, we can see that the huge disparity between them and us has somewhat waned. In some cases, they are actually losing staff at the moment—not necessarily in core tasks, but in some of their support functions. We feel better about the place we are in.

Q7 Clive Efford: How does 3% compare with the people you are competing with for staff? What do you anticipate the pressures being?

Gareth Davies: It is a prospective figure, so we do not have any data yet for their 2024-25 plans, and we will not have it for a while. Part of the problem is that benchmarking is always backward-looking on pay awards.

Our benchmarking on grade by grade shows that it is only when you get to the most senior grades that we are significantly off the pace in comparison with the same sorts of role in the firms. Given that our retention activity is highly focused on newly qualified auditors, that feels like a robust position for us.

Q8 Clive Efford: In the PAC evidence session, there was discussion about the specialisation of NAO staff. Do staff still work across the portfolio, or is the distinction between value for money and financial audit staff more stark than it was before?

Gareth Davies: That is a really interesting development. Both disciplines have become more specialised, but it is really important to us, and one of the strengths of the NAO's work has been the crossover between the two. We are determined to retain that while not compromising on having the specialist skills that we need for both types of work.

The specialisation in financial audit has been coming into technical areas. We now have a significantly higher number of people with pensions audit expertise, property valuation expertise and so on.



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On the value for money side, it tends to be more subject matter expertise, such as digital experts, procurement experts and so on, but the principle is the same: we need a core of generalists supplemented by increasingly strong pools of expertise, and we have developed pathways for people to move in and out of those areas of expertise. Training with us as an auditor gives you a generic set of skills, but we also now have clear pathways for people who are interested in becoming a technical expert, a pensions expert and so on.

That will include crossing over into the value for money area. Our hubs, which are where we gather our value for money expertise on subject matter, are now combined teams of people with a financial background and a value for money background. That is how I think we will maintain the crossover that you mentioned.

- Q9 **Clive Efford:** Having value for money staff focusing on supporting Parliament instead of financial auditors presumably risks parliamentarians missing out on insights from financial audit work. Have you considered that risk? If so, do you intend to mitigate it?

Gareth Davies: I do not think that that risk is materialising. What it means in practice is that the business of responding to Committee requests for briefings and so on is largely now falling on the shoulders of our value for money teams, particularly at a time when our financial audits are at full tilt.

On your question about financial audit expertise, we have developed some very popular briefing sessions on how to read Government accounts, for example, which are led by our financial auditors, and we have offered them to Committees, individual Members and research staff in Parliament. Those sessions have proved very popular, so we continue to offer them.

Dame Fiona Reynolds: It is also really important that the audit staff feel that they are offering insights, not only to the PAC but to the Departments they work with, because there is certainly a need for their insights and they are much appreciated.

- Q10 **Clive Efford:** Daniel, you mentioned in the PAC evidence session that the NAO wanted to pilot emerging technologies last year, but that that was moved to this year. Can you elaborate on the emerging technologies that you are exploring?

Daniel Lambauer: Yes. We are doing a range of pilots in analytics and also a little bit in artificial intelligence-supported tools, particularly for the audit side. These are either tools that help us to better ingest data on an organisation first, then analyse it, or to manipulate the data in-house or analyse it in-house once we have it.

Basically, what we do with all these tools is have a small-scale pilot first—a proof of concept to see whether it works and what we need to change—and then slowly ramp it up. We have done it with the audit transformation programme.

The plan was always to start the pilots towards the end of the financial year, so it is moving just by three or four months on the other side. That gives us a bit more time to think about what is needed and then make the investment.

Q11 Clive Efford: Why did you shift it back?

Daniel Lambauer: It is partly workload, but also partly because we looked at prioritisation for the year, as we explained in the last session. Overall, it will not make a massive difference when these tools are implemented; it is more that the pilot phases have moved a little bit to the right.

Q12 Jack Brereton: The letter that we have received from the Treasury has identified that the NAO faces a number of cost pressures. Are you confident that the measures that you have put in place to address those cost pressures will mitigate them?

Gareth Davies: Yes. I might bring Daniel in on some of the points of detail.

Essentially, like everybody, we have faced higher inflation costs outside the staff costs, particularly from our contracts with the firms. We describe in the paper the two main areas in which we work with the firms. The first is where they deliver whole audits for us, particularly in sectors where they have specialist expertise and we do not; we also rely on them through framework contracts for technical advice on things like valuations, model audits, questions and so on. In both cases, we have seen significant cost pressures coming through.

Part of our response is to ensure that we are buying from the firms only where we really require it. We have done that for a long time, but we are strengthening our processes around it. However, sometimes audit quality requires us to get that expertise, and we must do that.

On the outsourcing of whole audits, we have had a more fundamental review of our strategy. The board has looked at that business case and has approved a medium-term shift to a lower level of outsourcing of our audits than we have had historically. About 20%, by value, of our work has been outsourced on the financial audit side. We are looking to bring that down to more like 15% over the next three years or so.

The reason for that is that we have done the maths, and we think that will produce a cash saving against the counterfactual, which is to carry on at that level of outsourcing. It will be cheaper for us to resource those audits ourselves, but acknowledging that we are taking on a greater resourcing risk means that we will have to strengthen our capacity. One of the reasons for the increase in staff numbers that you have seen in the plan for next year is the beginning of that preparation for being able to take in more work.

This is not a situation in which we are doing that against the wishes of the firms, either. We have a shared analysis here that it is not very efficient



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for us to outsource straightforward, smallish public bodies. We are actually more efficient at auditing those, and it does not require specialist expertise in particular sectors.

We should be focusing our outsourcing. For example, we are now auditing organisations that are pretty much specialist insurance businesses; I am thinking of Pool Re and organisations of that kind. Where we are resourced to carry out audits ourselves, we are challenging whether we should be outsourcing those things and bringing in a larger number of smaller audits that are straightforward and more efficient to do ourselves.

This is a “steady as she goes” policy. We are doing this in stages, but I think the value for money case is very clear. Fiona may want to comment on the board’s perspective.

Q13 Jack Brereton: Do you believe that the actions you have taken thus far will be sufficient to address the issue?

Gareth Davies: We do, yes. We will always be exposed to some level of cost inflation in the private sector audit market. Our job is to ensure that it is no more than absolutely necessary. I think that we are taking the right measures on that.

Dame Fiona Reynolds: There were two very strong issues, from the board’s perspective. The first was the overall financial case. As you have heard, it is very clear that we are better at doing certain kinds of audits rather than outsourcing them. We also want to be able to equip ourselves with skills in response to the generally more complex requirements of audit. You cannot leave that all in the private sector; there was a very strong sense of that.

The other issue was about our feeling that it is in the best interests of the National Audit Office in the long term for people to acquire those skills and develop career opportunities to become more specialist, while retaining some capacity to learn from the firms and to outsource at the extreme end of specialism as we go forward. It felt like the right thing to do, both financially and for the development of the office.

Q14 Chair: How long do you expect the process of transitioning from 20% to 15%, which is your new target, to take?

Gareth Davies: Three to four years. The key moment is when our framework contract comes to its end. It is essentially a “three plus two” framework contract—there are three years in the main contract, and it is extendable for two. We plan to use those extensions, and each time we extend we will bring a small number of audits in-house.

With the re-letting of the contracts, the crucial thing is to ensure that this remains attractive work for the private sector—it is at the moment, and we need to maintain that. I envisage having similar-sized packages of work but with larger audits in them, with probably one fewer firm working for us than we have now, so that there is still a meaningful amount of work for each firm. That is important.



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Q15 **Chair:** Presumably, it is in your overall strategic interest to maintain a capacity in the private sector to offer work, which you buy from them.

Gareth Davies: Particularly given the disruption in the local government audit market and, to some extent, the NHS audit market, it is really important that we are a point of stability in the public sector procurement of external audit.

Q16 **Chair:** You mentioned the Pool Re insurance company. A number of other bodies were listed in your progress update memorandum, including the Independent Commissioner for Reconciliation and Information Recovery in Northern Ireland. Why is the Northern Ireland Audit Office doing that?

Gareth Davies: They are going to have a substantial London presence, as I understand it. The particular sensitivities around that organisation meant that the legislation required the NAO to be the auditor rather than the Northern Ireland Audit Office.

Q17 **Chair:** And it was best done from, as it were, a slightly greater distance.

Gareth Davies *indicated assent.*

Q18 **Chair:** You mention local government audit. Paragraph 2.19 of your memorandum says that “the C&AG has committed to consider using his code powers as part of a wider set of actions co-ordinated by DLUHC, with the FRC, to support the local audit market”. It also says in the preceding paragraph that the PAC had said “that DLUHC had not set out an overarching plan to address pressing problems and described a pattern of “shockingly late audit opinions’.” What code powers might you use? Can you say a bit about how that might pan out?

Gareth Davies: The situation, as we have said at previous sessions of the Commission, is unacceptable. In local government audit, we have big delays in signing audited accounts and that is at a time when the sector is under extreme financial pressure, as everybody can see. It is urgent now that action is taken to correct that position.

The Government are consulting on their own proposals to introduce a new statutory deadline by which audited accounts have to be published. It proposes a staggered series of those deadlines to gradually bring the timetable back to where it should be, over a period of years. The first deadline is proposed to be the end of September 2024, and that would be to clear up any outstanding opinions from 2022-23 or before. We have been working closely with the Government, the FRC—the other major player in this—CIPFA and others on the detail of the proposals. It is necessary to update the code of audit practice to reflect this new statutory deadline because that is not how it works at the moment. The code needs to reflect that.

Essentially, our changes are facilitating changes to allow the Government’s central proposal to be implemented. We are also working closely with DLUHC and the FRC on whether more detailed guidance will be needed to support that. Assuming that the changes are implemented by statutory instrument at the end of the consultation, we think auditors may well need



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more detailed guidance to ensure that we get consistent implementation of this. Clearly, there are some big risks here because the impact of the deadline will be to require auditors to produce whatever opinion they can at that deadline—hopefully, a completed audit. In cases where they cannot give a completed audit opinion, they will have to qualify or even disclaim their opinion on the accounts. That is clearly unsatisfactory for differences to emerge in practice between the firms on that very sensitive matter. For a council to get a disclaimer on its accounts is potentially a serious matter. That will need very careful management by Government, the FRC and other players in the system.

Q19 Chair: What is the root cause of this? Is it all a backwash from covid?

Gareth Davies: No; the roots of this predate covid. Covid made it worse, but this is a perfect storm of, essentially, the end of the Audit Commission. There is no single body overseeing all the aspects of the market and there is a fragmented set of responsibilities. That was all laid out in Sir Tony Redmond's review three or four years ago. That meant that different organisations were taking decisions about commercial contracts for that audit work. The regulatory approach, the quality approach—it was all fragmented. That made it very difficult to hold the ring properly on this. The FRC is now the shadow system leader as a direct response to that report.

That destabilising change in the local government audit world coincided with the big push on auditing standards that we were talking about earlier. The firms' approaches to regulatory intervention were significantly more risk-averse. Things they were very prepared to do for decades, they were suddenly not prepared to do in the local government context.

Q20 Chair: Because there is too much risk exposure?

Gareth Davies: Yes. Finally, the general financial pressure on local government has also affected the quality of financial teams preparing the accounts. This is a system-wide problem; it is not just located in one part of the forest. What is needed is a concerted effort to improve local government accounts and make them more relevant, simplify some of the unnecessary complexity and return the audit regime to the robust position it used to be in. This used to be a dull and reliable area of audit work, and it needs to go back to being dull and reliable. There needs to be proper attention to ensuring that this does not happen again in the future.

Q21 Chair: Didn't the Treasury try to introduce an office of local government oversight or local government reform—a sort of mini Audit Commission—three or four years ago?

Gareth Davies: That was Sir Tony Redmond's recommendation.

Q22 Chair: Did the Treasury not then push it?

Gareth Davies: I do not know the intra-Government debate on that recommendation. I do know that the Government did not accept it in the end, and that is a shame. I think it got to the heart of what was required



to hold this regime together. But we are now on a different track, so we need to make this work.

- Q23 Chair:** One of the things that concerns me is that if private sector firms are simply not interested in the work any more, and the National Audit Office has to stand as some sort of backstop, will that have a financial consequence for you? If this is work the private audit firms are not prepared to do, how would the NAO get involved in a way that was financially acceptable to the Office?

Gareth Davies: That is a very big question. We do not have the powers to do that at the moment. That is the simple answer. We certainly do not have the capacity. As you can see, we are at full stretch covering our existing set of pretty onerous audit responsibilities. Speaking frankly, there was a reason we had two organisations, one covering central Government and national bodies and the other covering local government and local bodies. In England, they are both very large sectors, and it would be a big distraction for the NAO to have to turn its attention to a sector that, while it has some similarities, also has some big differences. Having worked in both sectors, they are each specialisms. It would take a very large effort to not just resource up for this work, but ensure that people had the necessary skills and sector expertise to do a good job, because it is different. My strong advice to anybody making policy in this area would be to come up with a solution that does not require the NAO to be part of delivering the audits, because I think that would be taking us off-mission.

- Q24 Dame Meg Hillier:** One of the problems with local audit is the health sector. We have seen the delay in the DHSC overall accounts and some concerns you have had about those. Could you outline what your concerns are, and whether you think the situation there is rescuable, as it is now seeping into—

Gareth Davies: The health audit system is part of the whole local public audit system. It is often the same teams auditing local authorities and NHS bodies. So disruption in the local government timetable has knock-on impacts on that, and that is what we have seen. It is certainly not in the same poor state at this stage, but there have been worrying signs of cracks in what used to be a very disciplined, reliable process. One of the consequences of the delays is that, even where firms are doing a broadly good job of getting the health accounts done, they are not quite as early as they used to be, and that is on the critical path for us giving our opinion on the consolidated NHS accounts and the Department of Health's accounts. If Parliament is going to receive timely assurance on health spending, which it should, there is more work to do to return the health local audit system to its previous position.

- Q25 Dame Meg Hillier:** Do you have optimism that that can be achieved, given the pressures in local government as well? It is a huge task.

Gareth Davies: It can be achieved; it won't be achieved in one go. With enough commitment and will—there will be some cost implications, no doubt—and if achieving that is a shared priority, it can be done, yes.



Q26 Dame Meg Hillier: Do you think it will get worse before it gets better in health?

Gareth Davies: I wouldn't like to say. This year has been the low point in terms of NHS trust and ICB audits completed by the deadline. We are hopeful that next year will be better. We may have seen the worst point, but an auditor is paid to be pretty sceptical—we will need to see the evidence.

Q27 Jack Brereton: I want to ask a bit about your capital spending plans. You have plans to refurbish your London offices; some of us on the Committee have visited your fantastic offices previously. Would you please detail whether you think those proposals are value for money?

Gareth Davies: We are trying to take our own medicine on asset management with this approach. As the Chair said, it is also an important part of our being an attractive and effective place to work.

On asset management, part of our response to the pattern of work that has been emerging since the pandemic has been to reduce the floor space that we require in the London office. We now occupy 55% of that space, giving us 45% to let to paying tenants. The process is well under way. We had a difficult year last year getting the tenancy signed up, but the property market in our bit of central London has improved since then and we are now in a very good position for the coming year—the year covered by this plan.

We have three new tenants contractually signed up; in two cases, they have already moved in. A fourth has given us a firm offer in the past few days and we expect to proceed to contract with that one. That gets us almost all the way to our budgeted income for next year.

Q28 Jack Brereton: Are your capital plans very much linked to attracting in new tenants?

Gareth Davies: They are very much linked to that. The feedback from the potential tenants was that they loved the building—as you say, it is an art deco masterpiece: almost like a character in the organisation—but that the entrance was overwhelmingly NAO-branded. So we are subtly adjusting that to make it more welcoming to the 45% of people who will not be working for the NAO, without losing our identity in that process.

For the space that we are occupying, which is where the bulk of our capital investment plan is focused, the works are essentially to reflect the fact that we are working differently from when the office was designed that way 15 years ago. Some things need replacing anyway—the carpets are wearing out. One of my messages to the Government in my annual speech in January was making sure that assets are properly maintained as a driver of long-term value for money. We must not let our building deteriorate in that way.

A level of work would be necessary anyway. We thought that if we were going to have some disruption, we should work out what we needed to do to better reflect the way teams are working now. Our strong view is that



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we need to bring our teams together in the interests of high-quality audit work. The banks of hot desks, which are essentially what we have in the working areas of our building at the moment, are not good enough. We still need plenty of workstations, but we need collaborative spaces, more meeting rooms and places where teams can work together.

That is the driver behind the refurbishment: to put into place the lessons we have learned from our new office in Newcastle, which has been a big success—it really has allowed teams to work together in a different way. That has created an appetite for that at the London office, too. That is the thinking behind the plan. Daniel, do you want to say anything else about the economics?

Daniel Lambauer: No—I agree with all that. I hate correcting my bosses, but we are renting out 55% of floor space, so it is the other way around. We have a lot of floor space to rent out and we have £3 million of income every year.

Q29 **Jack Brereton:** Are you confident about reaching the target?

Daniel Lambauer: Yes. As Gareth absolutely rightly said, we have had good success in the last month. We are now on target to have four new tenants; we have three tenants moving in and one agreed terms just the other week. There is a lot of interest in the two remaining floors that we have to rent out over the next two years. I think the market has settled. We have made changes, as Gareth explained, to make the building more attractive. We have worked with our agents as well, as we talked about before, to have better marketing material. We are also working with the Government Property Agency to see where we can work within (vet) the rules, and perhaps have Government bodies or parts of Government bodies in the building. We are making good progress, compared with the last time I was here, when it was not looking that good.

Q30 **Jack Brereton:** You said quite a lot of work will be going on. What are you going to do to ensure that does not disrupt the important work that your staff undertake?

Gareth Davies: The beauty of having those newly vacated floors in the wing of our building is that we can use them as decant space for the teams. Essentially, we take a floor at a time for refurbishment, move the team into one of the vacant ones, refurbish, move them back in. Obviously, we are equipped to be mobile anyway, so very limited changes are required for IT capability and so on, because these are all our offices anyway. We do not need new security—

Q31 **Jack Brereton:** That suggests that you are not going to fill those additional floors.

Gareth Davies: Until the work has gone away.

Q32 **Jack Brereton:** But you are basing your budget on trying to get that rental income from those floors.

Comment [LD]: I am sure I said "within the rules"



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Gareth Davies: The £3 million that Daniel talked about excludes those two decant floors, until we get to the end of the work. The work will take two years, as we do floor by floor. At the end of those two years, we will let out those two remaining floors. There will be a further boost to our income, assuming the market is still strong at that point. There will be a further boost to our income at the end of that two-year programme of work.

Q33 **Jack Brereton:** So, you are not currently marketing those two floors?

Gareth Davies: No.

Q34 **Jack Brereton:** I would just ask a further question of Daniel, on the evidence given to the Public Accounts Committee session about the need to invest in cyber-security, and some of the challenges around that. Could you give a few more details about that and its financial implications?

Gareth Davies: May I start, and then I will bring Daniel in? I just want to say that in previous meetings of the Commission, you have correctly asked us in our annual report and accounts about the high-risk rating we have attached to cyber-security, and whether there is more that we can do about that level of risk. We take that incredibly seriously. You only have to see what happened to the British Library in the past six months, to see how catastrophic a successful hacking attempt can be for an organisation.

Our view is that we can have much better defences against that, and we should continue to build them, but we cannot have 100% guaranteed defences against it. That does require us to spend more on data loss prevention, ensuring that data cannot accidentally or deliberately exit the organisation, as well as preventing hostile attacks from outside. Daniel might want to expand on what we are doing on both of those.

Daniel Lambauer: That is totally correct. Just to say a little bit more about the threat environment, it is not too dissimilar to many other equivalent organisations. We are seeing increased and more efficient phishing attacks.

There is always the risk of data loss, as Gareth outlined. We have a more complex digital estate, which we need to patch and put security updates on. Software companies are pushing out more security updates that we need to maintain. That obviously costs money as well. We could also be targeted, as any organisations are targeted, in hacking attempts.

We are doing more on data loss prevention. On data management At the (management) space, we are bringing in new technical controls as well. We are still doing more to educate the organisation on phishing attempts, and we do more on identity management, to ensure that only the right people log into our system. We have controls that allow you to control who can log in and who cannot.

Comment [LD]: I thought I said "data" management



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All organisations now have to assume that there could be a breach and a loss. We are doing more on disaster recovery as well, looking at our back-up options, ensuring we have proper disaster recovery plans, in a world where we are now almost 100% cloud-based. Those are the main areas of investment.

Q35 Peter Grant: Mr Davies, can I go back to your earlier answers about the logistics of the decant when the work is being done in your offices? The way that Parliament operates, you will effectively only get your budget confirmed once a year, but you will also have a medium-term financial strategy over several years.

Over that type of timescale, if for any reason the refurbishment work is delayed, it may not only increase the cost of that work, but you will then be forgoing the income from part of your building for longer than intended. How big a potential problem does that create? How confident are you that the work will be done on time, so that you will get this other space let when you expect to?

Gareth Davies: On the confidence point, we have in-house a really effective project team with well-established contractor relationships for this kind of work. That has just recently proved to be very effective on the Newcastle office. The same team is responsible for these changes, so I think we have a very effective and reliable team there. The fact that, as you say, there is a double impact—not just extra costs but lost income—just acts as a very strong incentive for us to manage the risk of any overrun very tightly and, as I say, we have done it successfully just recently, so we think we can manage that.

If we did hit difficulties of that kind, we clearly would have to reprioritise in the way we have described some reprioritising of expenditure in the last year and, as a very last resort, come back to the Commission for a supplementary estimate if we had no other recourse. Given that this is down to our risk management, I think it is very unlikely that we would want to do that. This is about us making sure that we do not end up in that position and that we are successful, not just in refurbishing but in our commercial strategy for finding the right kind of tenants.

Q36 Peter Grant: Your main contractor and their subcontractors are going to be very well aware that any delay can cost you quite a bit of money. I am not asking you to reveal details, but are you confident that the way in which the contract is let will place a very, very firm responsibility on the contractor to deliver on time and you will not find yourself in a position where they have got you over a barrel and you have to agree to additional payments just to get the job done?

Gareth Davies: Yes, we are, because we have been in exactly that position in Newcastle recently and a highly effective contract structure worked—works—well there. Daniel, I don't know whether you want to comment.

Daniel Lambauer: The first thing to say is that we obviously wait for your approval of the budget before we even start the procurement process, so



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we do not have contractors in place yet. Everything is ready to go out for procurement, but we do not have them in place. In terms of the actual refurbishment, I think some of you have seen the Newcastle office. That was a substantial refurbishment of the floor, because we also built meeting rooms etc., which can obviously be trickier. We are not doing the full scale here. We are keeping the existing meeting rooms, so it is primarily furniture and some wall changes and some kind of IT equipment changes. Given that it is not so complex a refurbishment as you could make it, and if we get the procurement right, we should have a good contract in place.

The other thing I would say is that we hired in Newcastle an external quantity surveyor to help us challenge the costs. That has been really effective. They go line by line through the entirety of the cost items. We are going to do the same here. In the experience in Newcastle, we based the budget on relevant costs; we got input from quantity surveyors. A good, competitive procurement process should mean that we can control the costs quite well.

Q37 Chair: I am very pleased to hear you have hired a quantity surveyor to go through it line by line. I am sure Dame Meg and her fellow Committee members would share that view.

I want to bring in Clive Efford to ask about your future strategy, but I have one more question about the property side of things. I think I heard you say that, among other things, you are talking to the Government property service and that future tenants might include public bodies. Obviously, you are likely to be the auditor of those bodies, or there is a possibility you will be. Does this create any issues for you?

Gareth Davies: Yes. There are very clear ethical standards around business relationships between auditors and the bodies that they audit, in any sector, including our sector. That puts quite serious restrictions on the Government bodies that we can contemplate as tenants. The core rule is that it cannot be a transaction material to either party. That rules out small public bodies. For example, we could not host an entire small public body on one of our floors, because that would be clearly material to them. It also means we could not let half the building to one Department, because that would be material to us. So, having these multiple tenancies—if they are public bodies, it tends to be a small part of the public body. We also are very reluctant to host the finance departments of any of the bodies, because that is the bit of the organisation that our audit teams work most closely with.

That is the fundamental ethical guideline. Then, of course, we have other mitigating controls. The team dealing with our tenants as commercial tenants is nothing to do with our audit teams. There is no relationship there at all. Our audit teams never have conversations with any audited body that happens to be a tenant about their tenancy. We have strict guidelines on what can be discussed in the public areas of the building—

Q38 Chair: I was about to say that it is true that the catering facilities—the



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cafeteria—are shared between tenants. Without getting dramatic, one can easily imagine conversations over macaroni or cups of coffee that may lead in precisely the direction that one would not want.

Gareth Davies: That is why a very strong bit of our ethical standards is confidentiality. That applies to public areas of our building explicitly, as it does to any other place. Fortunately, most people want a break from auditing when they go and have their lunch. Most of the conversations are about the football and other things, rather than the intricacies of each audit. But it is a serious point. An important part of our controls is professional confidentiality at all times when you are not in your own office.

Q39 **Chair:** Presumably, because you have enough potential private sector demand, it is not a given that you would actually have a public sector tenant at all.

Gareth Davies: No, and that would be our preference, frankly. Clearly, the credit checks have to be more intensive on operators that we do not know—

Chair: We will see about that after the Budget.

Gareth Davies: Not backed by the taxpayer. Everything being equal, we would rather avoid any of those complications. What we learned last year was that effective engagement with the Government Property Agency has allowed us to fill one or two slots where the private market was not responsive. That has been a useful supplement. But you are right that our preference is to avoid all of those completely.

Q40 **Clive Efford:** What lessons do you take from the last four years in terms of the resilience of your strategy to unforeseen events? Are you planning your strategy for the next four to five years, and how will you engage Parliament in that process?

Gareth Davies: The timing was quite extraordinary. We published our strategy in March 2020, just as the pandemic was unfolding. We decided to press on because the strategy was not topic-specific—even a big topic like that. It was more thematic; it was about how the NAO plays its role to maximum effect. That turned out to be very useful, even—or maybe especially—in the circumstances of the pandemic.

The big change over the last four years in terms of the impact and resilience of the organisation is that we have delivered on our commitment to make better use of our knowledge. That is the big, central push that we have made over that strategy period. You have seen lots of the effects of that. I think we have been able to support the Public Accounts Committee with stronger analysis of what is required at the centre of Government on things such as digital transformation, commercial procurement, and even leadership and people management. I think those are now much stronger offerings from the NAO, because we have been able to synthesise the learning from our various reports on individual Departments and come up with a stronger analysis on improvements required centrally. It also

allowed me to make a speech in January, here in Parliament, which had a significantly greater impact on how the Government were thinking about some of these topics than previous efforts to bring together our findings.

There is good evidence that that strategic push has paid dividends. Clearly, there are other big parts of our resilience that we have worked on. We have talked about the audit transformation programme; I think that is the single biggest programme over that period of the strategy. Despite the pressures we have at the moment, as I have already said, about regulatory feedback, without that programme we would be in a significantly difficult position. That has laid the groundwork for substantial improvements in our audit quality as well. Those are the two I would pick out. Of course, they are supported by a big effort internally on people management, culture, and financial management. You have been hearing about some of that today.

Looking ahead, we are very keen to engage Parliament, and specifically the Public Accounts Committee, the Public Accounts Commission and other Select Committees, in our strategic thinking. We exist to support Parliament primarily, so what Parliament wants from us is fundamental to that strategy. Given where we are in the electoral cycle, we are very keen to talk to as many long-serving members of PAC and the Commission as possible before the election. We will then engage with the new Commission and the new Committee after the election as well, so we get both people who have worked with us for a long time in recent years and will have a lot to say about what we can do differently and better, as well as listening to the views of new Committee members who we will be working with through the lifetime of that strategy.

Q41 Chair: You will obviously have a lot of new Members of Parliament, who may or may not join the Public Accounts Committee or this Commission. How do you ensure that an entirely new cohort of Members of Parliament, of all parties, know about the NAO? My own experience as a young MP, 20 years ago, was that actually there were quite a lot of people who had been around here for a while but did not really know about what the NAO did.

Gareth Davies: Through our director of parliamentary relations, we have a plan that is ready for engagement with new Members of Parliament after the election. We are actually working very closely with the House authorities as we develop that plan. They have been very good, actually, about giving us access to induction processes and events. We are also very conscious about not overwhelming new Members. When you are preoccupied with finding an office and recruiting your staff and so on, you do not want mountains of emails. However, neither do we want to leave it too long before introducing ourselves and, particularly, how we can help and the support we can provide.

Q42 Clive Efford: So how do you go about consulting Parliament, and Members in particular?



Gareth Davies: Well, I am going to propose a workshop-style discussion with PAC members and Commission members. We have already had one workshop session with the Clerks of Commons Select Committees, including the PAC Clerks, and we had a really useful set of input from them. However, obviously, we want to do that with parliamentarians as well. I think that those are better done as informal sessions, rather than as public meetings of the Committees and the Commission, just so that we can get some real warts and all feedback on how we can deliver this essential task as effectively as possible. Then, as I say, we will do the same with new Members once they join.

Q43 **Peter Grant:** You may have answered part of my question. You mentioned induction for new Members. Will you be taking part in the wider induction that has been organised? There is work going on already, so will you have a slot somewhere in the bundles of parliamentary inductions?

Gareth Davies: Yes, that is the plan.

Peter Grant: Regarding longer-standing Members, who obviously will not go through the induction again, how good of an understanding do you think MPs who have not been involved with either the Commission or the Public Accounts Committee have about what the role of the NAO is and is not? I know, from some of the comments that you have made to the Public Accounts Committee, that you are sometimes having to turn down requests from Members for work that they think is part of your job, but either is not part of your job or is just not something that you can devote the resources to doing.

Gareth Davies: We find that awareness of us builds up over the life of a Parliament. We track that with an annual survey, which is revealing and useful, actually, on levels of awareness of what the NAO does, how to access us to raise topics of concern and so on. I think that the constraint on our ability to respond to individual Members is capacity.

Actually, I think we do a good job—and that is what the feedback tells us, actually; people think that we do a good job of responding to correspondence and to queries. Sometimes, that is to help to resolve an individual constituency query. More often, it is more of a thematic concern about a particular public service that is giving concern and so on. We do our very best to respond constructively to those; if it is within our remit and we can allocate sufficient resources to do a proper job, we do our very best to respond to those. Every year, actually, quite a long list of the NAO's outputs are as a direct result from an approach by a Member of Parliament, either a Committee member or not.

One of my jobs is to make sure that we are sufficiently responsive to those requests, but also that we have a strategic planned programme that covers the big risks to value for money. Holding that balance is one of the things that we spend the most time on throughout, because we could go too far in either direction, and that would cause its own problems.



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So, I am sure that you would find MPs who thought, "Well, I really would have liked the NAO to do a piece of work on that and they haven't been able to," but I think that more would say that they had had a good interaction with us, and either a constructive response with a piece of work or a clear explanation of why that was not possible.

- Q44 **Chair:** In recent times, there has been the abolition of two Government Departments and the creation of three new ones. In a report based on studies of reorganisation between May 2005 and June 2009—quite a long time ago now—Sir John Bourn, one of your predecessors as Comptroller and Auditor General, said, "The machinery of government is in constant turmoil—new departments and authorities being set up and older ones shut down or amalgamated." That churning, which involved over 90 central Government Departments and arm's length bodies—over 20 on average each year—cost in gross terms £780 million, equivalent to £15 million for each organisation. Now we have had these recent changes, which you are very familiar with and referred to in your memorandum. What advice would you have for any incoming Administration about more machinery of government changes?

Gareth Davies: My advice would be, first, set a high bar for such changes. Sometimes they may be necessary; I think everyone accepts that, but the burden of proof is on those proposing the change to explain why the benefits will outweigh not just the financial costs but the disruptive costs of energy and bandwidth from senior people. Those costs are always underestimated. The strong feedback that we get from everyone who has had to make these changes work is that, first, we should set a higher bar for any changes and we should be absolutely clear that they are going to make a big improvement. Secondly, when we do it, we should have a robust estimate of the financial costs incurred, and crucially the staff time costs, and make sure that is evidence-based rather than wishful thinking. That is really important, because all the evidence says that that is underestimated.

We are about to contribute more to the gathering pile of evidence on this question. In late March, we are publishing our report on the merger of the Foreign Office with DfID into the FCDO. We have looked at the various strands of activity that have been required to achieve that merger. I will not try to pre-empt the findings of a report we have not published yet, but I wanted to note that there is some more evidence coming. I think it backs up the general point that there are clearly advantages to be obtained through such changes, but there are very significant costs to staff time and energy. My final bit of advice would be to codify and develop guidance to support people who have to manage these processes, because at the moment there isn't anything like that.

- Q45 **Chair:** Wouldn't you expect the Cabinet Office, as part of its remit to help ensure value for money, and the Treasury, to have such guidance in place?

Gareth Davies: It should, and it should be more practically useful than it currently is. The direct feedback from senior people who have had to make



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these changes work is, "Why are we having to work all this out for ourselves when it has been done many times?". There is a clear requirement to bring together that good practice, and to help people do this faster and more efficiently.

Q46 **Chair:** Are you taking the trouble to draw these points to the attention of the centre of Government?

Gareth Davies: We will be.

Q47 **Chair:** Apart from your study on the FCDO and DfID, will you be exploring the broader question more thematically? Presumably, the new Departments that have been created and the old ones that have been shut down in the last 12 to 18 months have established enough of an evidence base over the last year and a half to be able to look at how it has gone.

Gareth Davies: Yes, obviously there is a fine balance between allowing them to get their new arrangements bedded in and asking to audit them, but it is an obvious topic for us, under the heading of thematic learning for Government, where we have something to add.

Chair: On that note, thank you very much for your time. We are very grateful. We will probably see you only one or two more times in this Parliament, but we look forward to that—perhaps after Easter. We are working on dates.