



National Audit Office

PAC 07

A decorative graphic consisting of two overlapping circles. The left circle is a dark maroon color, and the right circle is a light grey color. They overlap in the center, with the maroon circle partially obscuring the grey one.

National Audit Office Supplementary Estimate 2023-24

Memorandum to the Public Accounts Commission

MEMORANDUM

by the
National Audit Office

DECEMBER 2023



**We are the UK's
independent
public spending
watchdog.**

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

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

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

In 2022, the NAO's work led to a positive financial impact through reduced costs, improved service delivery, or other benefits to citizens, of £572 million.

Summary

1 This memorandum sets out the resource and capital budget changes the National Audit Office (NAO) is asking The Public Accounts Commission (the Commission) to approve. These being:

- £1 million (resource) owing to increases in the scope of the NAO's audit work prompted by 'machinery of government' changes announced in February 2023 covering both financial audit responsibilities and value for money assessments.
- £0.8 million (resource) to fund additional work needed to complete Parliament-funded audits in line with international standards. This covers audits where unavoidable and significant additional costs have been incurred to resolve issues arising during audit fieldwork, and which must be addressed before the accounts are certified.
- £1.9 million (resource) as further budget for pay following a decision to be consistent with the Civil Service pay guidance issued in June 2023 and make a £1,500 non-consolidated payment to junior staff and conclusion of the implementation of our new pay framework for staff.
- £0.5 million (capital) reduction in IT and equipment asset purchases originally planned for 2023-24 but which have now been rescheduled for 2024-25.

2 The memorandum also identifies a shortfall in our planned rental income for the year due to factors in the external property market affecting the demand for office space in London. However, we will fund this by careful reprioritisation of our business support activities and are not requesting funds in this supplementary estimate for this shortfall.

Background

3 The key priorities of the NAO continue to be our ongoing assurance and audit work, allowing us to discharge the full range of the Comptroller & Auditor General's (C&AG) statutory functions for Parliament and to act as the UK's independent public spending watchdog.

4 This Supplementary Supply Estimate for 2023-24 has been prepared to ensure that the NAO has the appropriate resource, capital and cash budgets to carry out our full range of work on behalf of the C&AG. These funds are used to employ staff, buy in outsourced services, pay for the travel costs associated with the work, and provide the infrastructure and support necessary to deliver work.

Summary of changes

5 The NAO is seeking funding changes in the current financial year as follows:

- An increase in the Resource budget for expenditure of £3.7 million.
- A decrease in the Capital budget for expenditure of £0.5 million.
- An increase in the Net Cash Requirement for expenditures of £3.2 million.

6 The overall impact of this request on the NAO’s Main Supply Estimate for 2023-24 is set out in **Figure 1**. Further information on the components of each request is included in the paragraphs below.

Figure 1

Main Supply Estimate for 2023-24 by budgetary limits

	Present Main Estimate	Supplementary Estimate Request	Revised Main Estimate
	(£'000)	(£'000)	(£'000)
Resource Departmental Expenditure Limit (RDEL)	91,100	3,700	94,800
Capital Departmental Expenditure Limit (CDEL)	3,700	-500	3,200
Net Cash Requirement	91,234	3,200	94,434

Source: National Audit Office

Changes to the Resource budget

Machinery of government

7 Machinery of government changes were announced in February 2023 and were not reflected in our Main Estimate. These changes abolished two departments – the Department for International Trade (DIT) and the Department for Business, Energy and Industrial Strategy (BEIS) – and created three new ones: the Department for Business and Trade (DBT), the Department for Science, Innovation and Technology (DSIT) and the Department for Energy Security and Net Zero (DESNZ) whilst also modifying the remit of the Department for Culture, Media and Sport. The three new Departments are supported by a large number of agencies and public bodies, with most of these part of the BEIS departmental group previously (**Figure 2**).

Figure 2

New Departments and their agencies and public bodies

Department	Number of agencies and public bodies
Department for Business and Trade	19
Department for Science, Innovation and Technology	15
Department for Energy Security and Net Zero	14
Total	48

Source: Departments, agencies and public bodies. Available at: www.gov.uk/government/organisation

8 The NAO has audited and certified the 2022-23 accounts for the legacy departments in the first half of 2023-24, with the accounts for DIT certified in July and BEIS' accounts certified in October. The changes mean that the NAO is also auditing the transfer of spend from the legacy departments to the new departments as part of its 2023-24 activity. In addition, we will be planning for, monitoring developments in, and auditing, one additional government department in 2023-24. The reallocation of agencies and public bodies across the three new departments means that more audit testing will be necessary. This is because the thresholds for determining whether expenditure has a material effect on the accounts of the new departments will be lower, as well as audit procedures now being required for three different consolidation processes to prepare the new departmental accounts, whereas previously the majority of agencies and public bodies were consolidated into the BEIS group accounts. We also expect to conduct additional report work and will publish 2 further reports for Parliament, targeting between 62 and 65 reports per year.

9 The NAO is therefore requesting £1.0 million in relation to machinery of government changes. This incorporates the recruitment of 10 FTE staff in 2023-24 (with a further 5 needed in 2024-25), the commissioning of external expertise as required, and travel and subsistence to support the audit of a new department and other audit procedures.

Financial audit

10 The NAO's financial audits are planned drawing on data and our experiences in the prior year and following discussions with the senior management of the audited bodies. However, the nature of audit means that further issues arise during fieldwork which require more work or additional expertise to resolve, or require the audited body to provide further evidence over a longer period to satisfy us before accounts can be certified in line with international audit standards. These issues add to the cost of our audit.

11 When additional costs are incurred on audits where the NAO charges a fee directly to the audited body (for example, bodies that operate at an arm's length from government) then we can adjust the audit fee. However, the NAO does not charge a fee directly to the audited body to recover these costs from our Parliament-funded audits and does not build in any contingency when preparing the annual main estimate for the Commission.

12 The NAO's external auditors, Crowe UK, considered these issues in its June 2023 review of our Financial Management of Financial Audit Work. It acknowledged that there were circumstances, external to the NAO, which led to audits costing more than anticipated at the time planning estimates were presented to the Commission. Crowe recommended that we either include a contingency in our Parliamentary supply estimate or seek direct recovery from departments in cases where audit costs are higher.

13 We discussed both these options with the Commission at its July 2023 evidence session on our annual report and accounts. In responding to Crowe's recommendations, the Commission Chair noted that the normal route in circumstances where audit costs exceeded the budget would be for the NAO to submit a supplementary estimate to the Commission. The Chair also expressed his concern that approaching a department directly for reimbursement could undermine the role of the Commission and risk the independence of otherwise Parliament-funded audits.

14 These costs are significant and necessary to complete the audits to the required standards, and to enable us to certify the accounts. They represent material changes that cannot be covered by moving staff and resources without a detrimental effect on audits elsewhere, or where specialist audit expertise has been necessary in light of the complexity of transactions entered into by the audited body. **Figure 3** summarises the most significant overruns from the NAO's Parliamentary fee audits and the reason that they have occurred. In line with the Commission's preferred approach, this supplementary estimate includes a request of £0.8 million in respect of Parliament-funded audits.

Figure 3

Main reasons for overruns from NAO Parliamentary fee audits

Cause	Cost overrun	Impact on audit
New areas of audit risk and focus arising after NAO audit budget setting and planning (for example, new financial guarantees being entered into by audited bodies during the financial year).	£0.2m	Required commissioning of additional specialist expertise to ensure audits met quality standards that have themselves increased in recent years.
Issues with the quality of information and audit evidence provided by the audited body, requiring more audit work than was originally planned (for example, sufficient quality audit evidence not being provided by audited bodies in line with agreed timetables meaning additional resources have been used to finalise audit work).	£0.4m	Required additional engagement with the audited body over a longer period of time, delaying audit certification.
Audited body transactions more complex than anticipated at audit planning stage, requiring additional work, also in the context of changes to financial reporting from April 2022 prompted by IFRS16.	£0.2m	Required commissioning of specialist external advice relating to the valuation of land and buildings to meet audit quality expectations.

Pay

15 The Commission will recall that at its March evidence session, the Chair invited the C&AG to confirm that he would, if necessary, return to the Commission with a supplementary estimate, following the conclusion of negotiations with the Union on pay-related matters. An agreement with the Union has now been reached which:

- Includes a one-off payment of £1,500 to staff below Senior Audit Manager/ Band 1 grade consistent with additional pay guidance for the Civil Service; and
- Implements the new pay framework for audit grades.

16 The Budget Responsibility and National Audit Act 2011 (the legislation that governs the NAO) requires that in determining the employment of any staff, the NAO must have regard to the desirability of keeping the terms broadly in line with those applying to civil servants. Therefore, the NAO carefully considers the Civil Service pay guidance in assessing our own pay approach. An addendum to the Civil Service pay guidance for 2023-24 was issued by the Cabinet Office in June 2023 after the NAO's budget for this year had been agreed. The addendum enabled departments to make a further, one-off, non-consolidated and non-pensionable payment of £1,500 to staff below senior civil service grades.

17 It is in this context that the C&AG has agreed, in principle, to make an equivalent offer to NAO staff. His decision also reflects staff concerns raised in the staff survey about pay and the cost of living. Inflation as measured by the Consumer Price Index (CPI) has been higher and more persistent than most expectations. CPI was at 10.1% in the 12 months to March 2023 and while now on a downwards trajectory and expected to fall further in the coming months, remained elevated at 6.7% in September 2023, mid-way through the financial year.

18 The budget for this one-off, non-recurring, payment is set out in **Figure 4** and included in the supplementary estimate.

Figure 4
One-off payment in line with Civil Service pay guidance for 2023-24

NAO staff below Senior Audit Manager grade (based on headcount)	Salary	Pension	National Insurance	Total
785	£1.2 million	£-	£0.2 million	£1.4 million

19 The final agreed pay framework for audit grades incorporates other modifications, in particular a decision to bring forward the appointment of all new audit manager grades to 2023-24, recognising that this would improve retention and staff morale while also reducing the period of change. The wider decision to create a new financial audit manager grade as part of the new pay framework reflects practice in the private firms and is aimed at improving our competitiveness as an employer and our wish to motivate, challenge and retain good professionally qualified people.

Income shortfall

20 The NAO’s rental income from our London office is expected to be lower than was anticipated in the Main Supply Estimate 2023-24. The NAO had planned rental income of some £2.2 million based on being able to rent out some 65% of our available space for letting in 2023-24, rising closer to 100% by 2025-26. However, we are now on track to rent out some 40% which will result in £1.4 million of income which is a shortfall of £0.8 million against plans.

21 This shortfall is because an existing tenant (a software company) unexpectedly exercised a break clause in its lease prompted by flexible home working arrangements which meant that it no longer needed the office space. In addition, our budget anticipated two new tenants for the year (an assumption reasonable in the context of previous experience before the pandemic) but which, despite robust marketing efforts and interest in the space, have not achieved the tenancy levels we had planned for.

22 The current uncertainty in the London office property market, prompted by organisations still determining patterns of office working post-pandemic and rising interest rates, is continuing to have an impact. Nevertheless, we remain confident that in the longer term we will achieve our aim of letting out all surplus space because our London office is in a good central location and offers a high quality of serviced accommodation.

23 We have carried out a rigorous internal budget review to identify where we can mitigate the impact of the loss of planned rental income. We have been able to reschedule training and IT initiatives which will be transferred to 2024-25; we have also been able to find permanent savings in our audit transformation programme by reducing the use of external consultancy in project management and transferring responsibility to NAO staff. This has reduced expected business support expenditure in 2023-24 by £0.8 million and is sufficient to offset the lost income. Therefore, the NAO is not requesting additional funding to cover the shortfall in rental income.

Changes to the Capital Budget

24 The NAO also intends to return £0.5 million in capital funding in 2023-24. This is to ensure that our procurement of IT equipment (desk top screens) is fully integrated with our wider plans to refurbish our London building space in 2024-25. We had also intended to upgrade the fire alarm systems this year in line with asset replacement plans based on standard expected useful lives. However, suppliers have been unable to carry out the work in this financial year and the NAO has rescheduled this to the next financial year. We have confirmed that the existing system can be safely maintained during the period of any delay to implementation.

Changes to the Net Cash Requirement

25 The net cash requirement of the NAO reflects the combined net resource requirement and proposed capital expenditure for audit and other assurance services after adjusting for non-cash items such as depreciation.

26 The changes requested to the Net Cash Requirement reflect the amendments to resource and capital budgets. Additional resource budget increases of £3.7 million will be incurred in the year and result in a cash outflow. However, the £0.5 million reduction in capital budget will reduce cash payments. Therefore, the NAO requests an increase to our net cash requirement of £3.2 million.

Approval of Memorandum

27 This memorandum has been prepared with reference to HM Treasury's Supply Estimates: a guidance manual. The information in this memorandum has been approved by the C&AG and the NAO Board. The Commission is invited to approve the NAO's Supplementary Estimate for 2023-24.