

# NATURAL ENGLAND AUDIT COMMITTEE

Paper No: AC/3/M1

NEB PO7 25 Annex 1

Title: Confirmed Minutes of the Third Natural England Audit Committee Meeting

18 June 2007, 12:30 – 15:45

**Present:** Christopher Pennell Chair  
Poul Christensen  
David Hill  
Ian Scott  
Pam Warhurst

**In attendance:** Helen Phillips Chief Executive  
Dave Webster Executive Director Finance and Corporate Services  
Helen Dixon Director, National Audit Office  
Steve Allen Manager, National Audit Office  
Mike Doughty Head of Internal Audit  
Paul Lambert Director of Finance  
Deborah Keith Manager Management Accounting and Reporting (Part)  
Claire Bullock Corporate and Resource Planning Team (Part)  
Emily Finnie Internal Audit Team Leader (Secretariat)

**Apologies:** None

## Welcome

The Chair of the Audit Committee welcomed everyone to the third meeting of the Natural England Audit Committee.

On behalf of the Committee, the Chair welcomed Ian Scott to his first meeting. There had been informal discussions before the formal meeting to explore how as a fifth (external) member he would bring his financial and accounting experience to the Committee.

The following interests were declared: Christopher Pennell was a member of the English Nature Council until Vesting and Poul Christensen is on the Defra Management Board.

## 1. Minutes of the Second Meeting of the Audit Committee held on 27 March 2007 (AC/2/M1)

1.1 The Committee **confirmed** the minutes of the second meeting of the Audit Committee without amendment.

## 2. Matters Arising (AC/3/A1)

2.1 The Committee noted that, apart from updates given below, the matters arising from the last meeting had been discharged or were covered by agenda items.

- 2.2 The Chair of the Audit Committee reported that he and the Head of Internal Audit had discussed Internal Audit Strategy and that he would send him comments. **(ActionCP)**
- 2.3 It was noted that the Board had delegated to the Audit Committee its role in recommending to the Accounting Officer that the Annual Report and Accounts be signed (NEB P07 18), and this would be taken at agenda item 5.

### **3. Statement on Internal Control (AC/3/P1)**

- 3.1 Dave Webster and Paul Lambert introduced the paper and invited the Committee to assess the extent to which their assurance report provided a sound assessment of the standards of internal control operating in 2006/07.

#### **Internal Control Questionnaire**

- 3.2 In discussing the results of the internal control questionnaires the Committee:
- 3.2.1 noted that the 18% who reported failure of controls for management systems was linked to lack of testing business continuity plans and preparation of diversity action plans;
- 3.2.2 noted Finance and Procurement's 21% score for controls failing was because the team was reliant on a third party (Defra Shared Services (SSD)) to deliver, and from whom evidence of the operation of financial system controls, reconciliations and management information was not available on a timely basis;
- 3.2.3 noted risk management, business continuity planning, diversity action plans, non-financial scheme of delegation, succession planning, control of assets and financial system of control were the areas where a number of teams had identified weaknesses in control that were considered for inclusion in the Statement on Internal Control, and that actions had been identified by the Executive Board, Executive Leadership Group and Heads of Teams to improve these.
- 3.3 In discussion about the service provided to Natural England by SSD, the Committee expressed concern about SSD's surprisingly optimistic response to the questionnaire which did not reflect the ongoing issues since Vesting, and the fact that the Service Level Agreement could not be signed because of problems in agreeing a matrix of performance measures. Both NAO's external audit and Defra's internal audit reviews of SSD had identified definite weaknesses in internal controls that were under discussion. Natural England would not sign the SLA until necessary assurances had been received. Dave Webster reported that discussions with SSD continued and the Committee advised that a marker should be put down with the Chief Executive for recompense for additional resources Natural England was providing and consideration should be given to not paying for the service. The fall back position and contingency plans were noted should the situation not improve.
- 3.4 In conclusion the Committee:
- 3.4.1 welcomed the internal control questionnaire exercise that had provided valuable material. It encouraged follow up through the agreed action plans monitored by management and reviewed by Internal Audit, but agreed that, at this early stage in Natural England's evolution, this did not warrant specific investigation by the Audit Committee;
- 3.4.2 accepted officers' comments that the results were not untypical for this stage in the organisation's development and would provide an important benchmark for comparison in future years.

- 3.4.3 recognised that inconsistency in the interpretation of the questions had resulted in variable scores between teams but this was to be expected when benchmarks for risk appetite and control frameworks were under development. Members encouraged officers to follow up providing a benchmark for Natural England rather than focussing on investigating discrepancies. Paul Lambert offered to seek an interim view in September and bring a report to the December meeting ;( **Action PL**)
- 3.4.4 resolved that if significant differences in questionnaire scores persisted in future years, the Committee would have to take a stronger view of the need to investigate those differences.
- 3.4.5 noted that the Head of Internal Audit would be reviewing and suggesting suitable standards for future years. Of particular interest were differences in controls that could be due to interpretation of responsibilities or role and differences in management style. (**Action MD**)

### **Statement on Internal Control**

- 3.5 Paul Lambert introduced the draft Statement on Internal Control and drew the Committee's attention to the Executive Board's decision to exclude diversity action plans and succession planning from the significant internal control issues identified in the document. In discussion the Committee:
  - 3.5.1 advised that in the light of its earlier discussion on SSD, the comments in relation to Natural England monitoring the quality of its bought in corporate services on page 2 should be strengthened;
  - 3.5.2 suggested that a joint risk register should be developed with the Joint Nature Conservation Committee as a contribution to good governance. Helen Phillips confirmed this would assist her in her lead Accounting Officer role. (**Action TD**)
  - 3.5.3 expressed concern about covering outsourced services and systems for which the Accounting Officer was responsible, noting the formal transformation process for Genesis was included in the strategic risk register. Dave Webster offered Ian Scott separate briefing on Genesis. (**Action DW and PL**)
  - 3.5.4 advised that there should be reference to the specific significant risks faced by Natural England and how they were being handled;
  - 3.5.5 recommended that the SIC should be made more kinetic. As currently drafted it underplayed the Executive team's achievements against the real challenges since Vesting in moving strongly towards clearer consolidated Natural England (as opposed to founder) controls;
  - 3.5.6 in the light of the internal audit report and NAO's findings on financial systems of control, recommended that the management action should include review of progress by the Audit Committee;
  - 3.5.7 agreed with NAO's advice that the SIC should include the Head of Internal Audit's opinion giving limited assurance (amber/red);
  - 3.5.8 requested that consideration should be given to including a reference to health and safety.
- 3.6 In conclusion the Committee endorsed the management assurance supporting the Accounting Officer's Statement on Internal Control. The Committee's assessment was that there were no further significant internal control issues that it would wish to bring to the attention of the Accounting Officer for disclosure within the Statement on Internal Control.

The Committee noted that the Statement on Internal Control would be amended in the light of its advice. **(Action PL)**

#### **4. Internal Audit Annual Report and HIA Opinion for 2006/07(including JNCC) (AC/3/P2)**

- 4.1 Mike Doughty introduced his formal annual report and opinion given to the Accounting Officer to assist in preparing the Statement on Internal Control, and to the Audit Committee to assist in advising the Accounting Officer on control matters.
- 4.2 The Committee noted that the Head of Internal Audit's opinion was that he could give a limited level of assurance (amber/red) that the control framework for Natural England was operating effectively. The Committee supported his judgement that but for SSD issues he would have given a moderate (amber/green) level of assurance. The Committee agreed with the assessment that despite some control weaknesses, Natural England's existing control framework (with its top-level Natural England controls and lower-level inherited detailed controls) was good enough not to endanger achievement of strategic and organisational objectives, but those weaknesses could have impact on systems or process objectives.
- 4.3 The Committee noted the Joint Nature Conservation Committee's report and HIA opinion provided to support the Natural England opinion.

#### **5. Annual Report and Accounts (AC/3/P3)**

- 5.1 Dave Webster presented the annual report and accounts for 2006/07 for review and approval, and tabled updated versions of both documents.

##### **Annual Report**

- 5.2 In discussion the Committee:
  - 5.2.1 commended officers' excellent work in producing a powerful document with positive messages arranged around outcomes and good case studies;
  - 5.2.2 welcomed the changes in the updated report that had been redrafted to adopt a sharper and shorter style but advised that the final version should be easy to navigate;
  - 5.2.3 advised that further consideration should be given to providing clarification that this was the first part of a 3-year journey;
  - 5.2.4 noted reasons why status against targets had been removed from the draft, but advised that the report should capture that it was the intention to include this information from next year;
  - 5.2.5 advised that in the next draft: checks should be made where quoting figures to ensure consistency between sections, the appropriateness of all pictures should be reviewed and consideration should be given to including a glossary;
  - 5.2.6 recommended that the declaration of Dovedale NNR, Natural England's first, should be included;
  - 5.2.7 advised that the Foreword should include magnanimous reference to the work of the founding bodies;

- 5.2.8 In conclusion the Committee noted that Dave Webster was convening an expert group on 21 June who would be asked to take on board the Audit Committee's advice in the next draft. Members agreed to send in any detailed drafting points to Dave Webster. **(Action DW and Committee members)**

### **Annual Accounts**

- 5.3 Paul Lambert and Debbie Keith explained the key changes and work left outstanding on the annual accounts.
- 5.4 The Committee discussed the implications of new Treasury accounting policy. Grant-in-aid was now shown as funding transaction rather than income which led to a deficit of £33m being shown on the balance sheet. The Committee advised that consideration should be given to seeking a letter of comfort from Defra, and that a note should be added to the accounts providing an explanation. NAO advised that clarification should be included in the operation cost statement. **(action PL and DK)**
- 5.5 The Committee noted the major changes in the tabled version included:
- Agreement with NAO on 2005/06 comparators
  - Directors' bonus information
  - Readjustment of £100k from a fixed asset to a grant and correction of an accrual of £144k that had been included twice
  - Reclassification of programmes on p38/39
  - Removal of notional charges of services for RDS
  - Reclassification of creditors, but a comparator was still being worked on for taxation and social security
- 5.6 In commenting on the annual accounts, the Committee:
- 5.6.1 advised that a note should be added to 6.2 on staff numbers;
- 5.6.2 queried the amount of information provided on remuneration, and advised that consideration should be given to presenting this at the end of the accounts. NAO agreed to explore this with its technical team. **(Action Helen Dixon, NAO)**
- 5.6.3 queried contingent liabilities in relation to legal costs and was reassured by Dave Webster's explanation;
- 5.6.4 recommended that there should be consistency in presentation of the information on Board members;
- 5.6.5 requested that non-operational heritage assets be given further consideration in relation to NNRS;
- 5.6.6 advised that there should be a separate note on loss or sale of fixed assets;
- 5.7 The Chair of the Audit Committee thanked officers for work on the annual accounts. The Committee was invited to send in any further points. **(Action Committee members).**
- 5.8 The Committee approved the report and accounts for signing off by the Chief Executive subject to any subsequent advice on matters arising from the Finance team's and NAO's further work from the Chair of the Audit Committee with Poul Christensen deputising as necessary in Christopher Pennell's short absence on leave. **(Action HP and CP)**

## **6. NAO Opinion for 2006/07 (AC/3/P4)**

- 6.1 Helen Dixon and Steve Allen gave an update on work in progress on NAO's work on the Natural England 2006/07 Annual Report and Accounts. The Committee noted there were likely to be some further adjustments in the following areas:
- Treatment of Grant-in-aid and associated balances
  - Presentation of pre-vesting balances
  - Disclosure of the use of Genesis and associated re-charges from Defra
  - Treatment of the transactions associated with the Natural England pre-cursor body and,
  - Re-classification of amounts currently presented as notional costs associated with RDS.
- 6.1.1 The Committee noted NAO's position at final audit on the 14 risk areas identified in its strategy, and in discussion:
- 6.1.2 noted actions in hand in relation to risks 1 and 2;
- 6.1.3 in relation to risk 3, agreed given the internal audit and NAO findings, that it would be negligent as an Audit Committee if it did not ask for a report from SSD. The Committee asked Dave Webster to invite the Chief Executive of SSD to the next meeting. **(Action DW)** Another element of assurance could be provided from Defra's Head of Internal Audit and Dave Webster would pursue this; **(Action DW)**
- 6.1.4 noted there were no specific risks remaining, and/or risks were being managed in risk areas 4-7 and 10-11;
- 6.1.5 noted in relation to risks 8 and 9, that NAO was content that the budgetary position for ERDP and the Rural Development Programme was agreed by all parties, and that issues in relation to Genesis were being managed;
- 6.1.6 noted NAO were still reviewing processes in relation to risk 12 ( co-ordination of end of year cut off procedures);
- 6.1.7 welcomed NAO's conclusion that subject to their further investigations, Natural England had put together a good quality annual report and accounts in difficult circumstances.

In conclusion the Committee noted that although the timetable for the final audit was two weeks behind, it was expected that the pre-recess timetable for signing of the accounts would be met. The Chair of the Audit Committee thanked NAO for its progress report. NAO reported that any further issues would be resolved as necessary via correspondence with the Audit Committee Chair. The Chair would report to the September meeting. **(Action CP)**

## 7 Risk Management (AC/3/P5)

- 7.1 Dave Webster introduced the update on risk management. In reviewing the format and content of the Natural England top-level risk register the Committee:
- 7.1.1 noted that failure to take advantage of opportunities was captured in all top level risks;
- 7.1.2 noted that the risk appetite for risk 1(failure to make the management arrangements complete, and consistent, understood and implemented) was reduced from high to medium as processes and systems became established;

- 7.1.3 expressed concern over implications of risk 2 (failure to deliver environmental stewardship scheme management to time and standard), but noted NAO reported RPA's improvements in the Rural Landuse Register;
- 7.1.4 noted that the risk of a change of government was covered in risk 6 (failure to align the Natural England strategy to Defra and Ministers);
- 7.1.5 flagged up the need for Natural England to be seen as more regulatory in relation to risk 8 (failure to deliver statutory responsibilities);
- 7.1.6 queried the low probability rating for risk 9 (failure to meet health and safety objectives);
- 7.1.7 advised that in relation to risk 10 (disruption caused by emergence of an external environmental factor) the risk that Natural England might not be able to get out to do its work should be included.
- 7.2 The Committee welcomed progress made since the last meeting (particularly in introducing the concept and use of risk appetite) and endorsed the risk management process. The challenge was now to get all staff to own the process and to get the 'bottom up' approach working as soon as possible. The Committee noted that at the September meeting it will have an opportunity to consider the results of risk management assessment to be carried out using the Treasury's Risk management Assessment Framework. **(Action:DW)**

## 8 Internal Audit Report (AC/3/P6)

- 8.1 Mike Doughty introduced his report which gave an update on the provision of internal audit services and activity. The Committee reviewed and noted progress on agreed work-plans for 2006/07 and 2007/08. In discussion the Committee:
  - 8.1.1 noted receipt of two final 2006/07 reports on health and safety and financial management that it would have the opportunity to consider formally at its September meeting. **(Action MD)**
  - 8.1.2 noted the two 2006/07 regional activity reports had been delayed because of difficulties in extracting information from SSD and separate IT systems, but that PKF now had the evidence to produce draft reports. NAO requested copies as part of their sign off of the annual accounts;**(Action EF)**
  - 8.1.3 supported the continuation of regional studies, to be co-ordinated with NAO, as part of the annual internal audit programme;
  - 8.1.4 noted work on Genesis would be undertaken as part of the internal audit programme if the Gateway 4 review was not sufficient to give assurance before Natural England accepted the system.
- 8.2 Dave Webster offered to arrange a separate briefing for Ian Scott on the Transition Programme **(Action DW)**
- 8.3 The Committee noted the additional control advice and support provided by Internal Audit.
- 8.4 The Committee reviewed and noted the full business process for internal audit that had been agreed by the Executive Board, and in particular its role in reviewing the implementation of audit recommendations, with a first full report coming to its September meeting **(Action MD and EF).**

8.5 The Committee noted and endorsed the update on resources, noting that recruitment was underway for the senior auditor vacancy, and that the contract for 2007/08 had been let to PricewaterhouseCoopers. The Committee supported the proposal to use the OGC framework contract for the procurement of an internal audit service from 2008/09 to 2011/12, and the Chair of the Audit Committee and Ian Scott agreed to be involved in the process as required.

## 9 **Fraud Policy and Procedures (AC/3/P7)**

9.1 Dave Webster introduced the paper that set out Natural England's anti-fraud policy and provided an update on fraud reporting including the annual report to Defra.

9.2 The Committee:

9.2.1 endorsed the anti-fraud policy, and noted that a workshop was to be arranged to test major areas of risk and to define mitigating controls; **(Action DW and MD)**

9.2.2 noted that while all staff had been informed about the whistle-blowing policy that was available on the intranet, there was further work to do in raising awareness through a series of control seminars planned for later in the year; **( Action MD)**

9.2.3 noted the update on fraud reporting.

## 10 **Audit Committee Forward Look (AC/3/P8)**

10.1 The Committee reviewed the meeting which it concluded had gone well. A final version of the accounts would have been helpful but all Members understood the timetabling issues that had prevented this being possible.

10.2 The Committee noted the programme of business for the next meeting on 10 September and agreed new dates for the following two meetings as:

Monday 26 November (pm) Sheffield

Monday 10 March (pm) Sheffield

## 11 **Any other Business**

11.1 There was none.

## Action Points

### Third Meeting of the Natural England Audit Committee – 18 June 2007

| No | Min ref | Action                                                                                                               | Responsibility                                | Action taken |
|----|---------|----------------------------------------------------------------------------------------------------------------------|-----------------------------------------------|--------------|
| 1  | 2.2     | Send comments on Internal Audit Strategy to Head of Internal Audit.                                                  | Christopher Pennell                           |              |
| 2  | 3.4.3   | Seek an interim view on internal controls questionnaire in September and report to December Audit Committee meeting. | Paul Lambert                                  |              |
| 3  | 3.4.4   | Review and suggest standards required in relation to the internal controls questionnaire for future years.           | Mike Doughty                                  |              |
| 4  | 3.5.2   | Develop a joint risk register with JNCC.                                                                             | Tony Dover                                    |              |
| 5  | 3.5.3   | Provide separate briefing for Ian Scott on Genesis.                                                                  | Dave Webster/ Paul Lambert                    |              |
| 6  | 3.6     | Amend the Statement on Internal Control in the light of the Audit Committee's discussion.                            | Paul Lambert                                  |              |
| 7  | 5.3     | Send any detailed drafting points on the annual report to Dave Webster.                                              | Audit Committee Members                       |              |
| 8  | 5.3     | .Report Committee's comments on the annual report to the expert group meeting on 21 June                             | Dave Webster                                  |              |
| 9  | 5.5     | Amend annual accounts in the light of Members' comments.                                                             | Paul Lambert and Debbie Keith                 |              |
| 10 | 5.7.2   | Explore re-ordering of the annual accounts with NAO technical team.                                                  | Helen Dixon, NAO                              |              |
| 11 | 5.8     | Send in any further points on the annual accounts.                                                                   | Audit Committee Members                       |              |
| 12 | 5.9     | Approve the final annual report and accounts.                                                                        | Helen Phillips advised by Christopher Pennell |              |
| 13 | 6.2.2   | Invite the Chief Executive of SSD to the next Audit Committee meeting.                                               | Dave Webster                                  |              |
| 14 | 6.2.2   | Seek assurance on SSD's service from Defra's HIA.                                                                    | Dave Webster                                  |              |
| 15 | 6.3     | Report on final NAO opinion to September meeting.                                                                    | Christopher Pennell                           |              |
| 16 | 7.2     | Present a paper on the results of the risk management assessment to the September meeting.                           | Dave Webster                                  |              |
| 17 | 8.1.1   | Present final internal audit reports to September meeting.                                                           | Mike Doughty                                  |              |
| 18 | 8.1.2   | Send copies of final internal audit reports to NAO.                                                                  | Emily Finnie                                  |              |
| 19 | 8.3     | Provide briefing on the Transition Programme to Ian Scott.                                                           | Dave Webster                                  |              |
| 20 | 8.4     | Provide a recommendation monitoring report to the September meeting.                                                 | Mike Doughty and Emily Finnie                 |              |
| 22 | 9.2.1   | Ensure arrangement of an anti- fraud workshop.                                                                       | Dave Webster/ Mike Doughty                    |              |
| 23 | 9.2.2   | Ensure awareness of whistle blowing arrangements are raised in forthcoming control workshops.                        | Mike Doughty                                  |              |