

Natural England Board

Meeting 7
10 October 2007



Paper No: **NEB P07 25**

Title: **The Audit Committee's First Annual Report to the Board**

Sponsor: **Christopher Pennell, Chair of Audit Committee**

1. Purpose

- 1.1 The purpose of this paper is to present the Audit Committee's first annual report to the Board.

2. Recommendations

- 2.1 It is recommended that the Board:
- note the Audit Committee's first annual report and the appended confirmed minutes of the Audit Committee's meeting on 18 June 2007 and the unconfirmed minutes of the meeting on 10 September 2007.

3. Background

- 3.1 The standard programme of Audit Committee business includes submission of an annual report to the Board at its June meeting. For this year only, the Chair proposes instead that the Committee gives its first annual report to the Board in October 2007, a year after Vesting.

This report includes a summary of the establishment of the Audit Committee and its business during the first year of Natural England. Copies of the December 2006 and March 2007 minutes have been circulated previously to the Board (NEB P07 07 and NEB P07 13). The minutes of the June and September 2007 meetings are attached at Annexes 1 and 2.

4. Establishment of the Audit Committee

- 4.1 The Audit Committee was set up prior to Vesting of Natural England as a standing committee of the Natural England Board established in accordance with Schedule 1 19.1 of the NERC Act. Its role is to advise the Board on matters of financial accountability, risk and internal control. Its terms of reference were agreed at the fourth meeting of the Skeleton Body Board on 13 September 2006.

Membership

- 4.2 In accordance with its terms of reference the Audit Committee comprises five members, four of which are members of the Board. The Board members are Christopher Pennell (Chair), Poul Christensen, David Hill and Pam Warhurst.

Ian Scott, an external fifth member, was appointed in June 2007 to meet the Treasury guidance that at least one member of the Committee has relevant financial accounting experience. In addition David Hill is a member of the JNCC Audit and Risk Management Committee.

- 4.3 The Chief Executive, as the Accounting Officer, is not a member of the Committee but attends all meetings along with the Director Corporate Services, the Head of Internal Audit and representatives from the National Audit Office.

Training

- 4.4 A tailor made training package was developed and delivered by the National School of Government in February 2007. Strengthened by this induction training that was based on the revised Treasury Audit Committee Handbook, the Committee has moved swiftly beyond an initial 'feeling its way' to fully meeting its objectives.

5. Audit Committee Meetings

- 5.1 The Committee met twice as a Skeleton Audit Committee. Key tasks were to make an input to its draft terms of reference and to advise on Natural England's requirements from the corporate governance framework, risk management framework and interim Statements on Internal Control. The Committee supported and strengthened the Accounting Officer's demand of the founding bodies that their stewardship statements and assurance packages for the first half of 2006/7 should be comprehensive enough to give her adequate comfort in preparing her eventual Statement of Internal Control for the full 2006/7 year. In the event, we had some concerns about the levels of assurance provided by the Rural Development Service.
- 5.2 Since Vesting the Committee has met four times in accordance with Treasury best practice. Half day meetings were held on 4 December 2006 and 27 March, 18 June and 10 September 2007 and, additionally on the latter date, the Committee also received informal briefings on the Transition Programme and on Genesis. All meetings have been well attended by members and supported by good papers from officers and the National Audit Office with whom good working relations have been established.

6. Audit Committee Business

- 6.1 At its first meeting the Audit Committee agreed its annual programme of business which now forms the standard agenda for each meeting to which additional items are added as required. The year's programme allowed the Audit Committee to meet its objective of assisting the Board to fulfil its corporate governance responsibilities through challenge, scrutiny, monitoring and advice to ensure that the control environment is maintained by Natural England. A summary of the outcome of the meetings is set out under the following headings:

Internal Audit

- 6.2 The Committee kept an oversight of the establishment of the internal audit function in Natural England. The appointment of Mike Doughty as Head of Internal Audit in March 2007 was welcomed and the continuation of internal

audit services from external providers by successive contracts from PKF (for 2006/07) and PricewaterhouseCoopers (for 2007/08) was endorsed, together with the plans for future longer term arrangements from 2008/09 to 2010/11.. The in-house team was strengthened further in August 2007 with the appointment of Peter Sleigh as senior specialist. The Committee agreed the terms of reference for internal audit and approved the risk based work plans for the remainder of 2006/07 and for 2007/08. Advice was given on the internal audit strategy and the internal audit process was noted, but the Committee has only recently begun to receive a flow of Internal Audit reports for its consideration.

- 6.3 The Committee noted that the Head of Internal Audit's opinion for 2006/07 (as provided to the Accounting Officer) was that he could give a limited level of assurance (amber/red) that the control framework for Natural England was operating effectively. The Committee agreed with the assessment that despite some control weaknesses, potentially impacting on the achievement of specific systems, functions or process objectives, 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.

Risk Management

- 6.4 Risk management is the area where the Committee has had the most significant impact. The Committee's advice focused on senior management digging beneath headline key risks to identify actions necessary to mitigate key risks and suggesting that the Executive should state Natural England's risk appetite. Implementation of these suggestions has contributed to welcome progress in embedding a risk management framework in Natural England which the Committee hopes will progressively have a bottom-up risk identification dimension as well as a top-down one. The strategic risk register of top level risks has been reviewed at each meeting and the Committee agreed it would take more comfort if the Board also took an in-depth look at the risk register which was subsequently done. The Committee welcomed the output from the Executive's application of the Treasury's Risk Management Assessment Framework to Natural England's risk management process.

Corporate Governance Framework

- 6.5 The Committee advised on installation of an overall governance framework. It welcomed the wide range of governance documents at Executive and Board levels and the amount of good work leading to their production before and after Vesting. Support was given to Natural England's objective of becoming an exemplar on corporate governance demonstrated by making documents available on the internal intranet and external website.

Statement on Internal Control

- 6.6 The Committee reviewed the assurance packages and Interim Statements on Internal Control from each of the founding bodies and endorsed the overall process for the Statement on Internal Control for 2006/07. It welcomed the controls questionnaire introduced as an additional part of the assurance process to help with the development of the Statement on Internal Control for 2006/07. The Committee endorsed the management assurance this process

provided in supporting the final Statement on Internal Control and it recommended that, after suitable amendment, it should be signed by the Accounting Officer.

External Audit and the Annual Report and Accounts

- 6.7 Helen Dixon and Steve Allen attended all meetings as representatives from the National Audit Office. The Committee received the audit strategy for 2006/07 and regular reports on the areas of audit risk identified. The Board, because of issues over timing of meetings, delegated to the Audit Committee its role in recommending to the Accounting Officer that the annual report and accounts be signed. This role was discharged at its June 2007 meeting with the Audit Committee approving 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.
- 6.8 The Committee was very conscious of the considerable difficulty and complexity for Natural England's Finance team in preparing accounts for 2006/7, the first half of which was managed by three different bodies. This difficulty was compounded by accounting service deficiencies from the Defra Shared Services organisation (SSD), such that the Committee determined to ask the CEO of that organisation to attend its September 2007 meeting. The Committee was also conscious of the challenge which the NAO faced in auditing those accounts, and, in the event, we were disappointed that the audit was not completed in time for Natural England's Report and Accounts to be laid before Parliament by the Recess. At its September meeting the Committee received an update on the current status of the annual accounts and discussion focussed on achieving an unqualified set of accounts at the first opportunity after the summer recess on 8 October. The updated position will be described orally to the Board at its October meeting.
- 6.9 At its September meeting the Committee received a presentation from Neil Serjeant, Chief Executive of Shared Services Directorate. The Committee was looking for reassurance following reports on SSD internal control issues from Finance, Procurement and Internal Audit, and National Audit Office's advice that this was a risk area in relation to its audit of the annual accounts. Concerns were compounded by the optimistic SSD response to the internal controls questionnaire. In the event the session deepened the Committee's concerns not just about SSD's ability to resolve existing problems but also about its capacity and efficiency in the longer term. The Committee will monitor performance at each meeting in future and has asked for options for alternative provision to be explored.

Other Business

- 6.10 The Committee supported Natural England's aspiration to become an upper quartile organisation for Health and Safety and welcomed progress with publishing and implementing Health and Safety policy. The anti-fraud policy was endorsed and the Committee advised that increased awareness of this and the whistle-blowing policy should be implemented through a series of control seminars to be held in the autumn.
- 6.11 On a personal note I would like to record my appreciation of the commitment and thoroughness of my fellow Committee Members in setting up the

Committee and in ensuring that it is both assiduous in its work and not over-sober in its proceedings. The Committee as a whole would like to express its appreciation of the many staff members who support its work, but particularly thank Dave Webster, Mike Doughty, Paul Lambert , Tony Dover and its Secretary, Emily Finnie, and thank Helen Dixon and Steve Allen of the NAO for their critical analysis of Natural England's activities. We additionally thank the Accounting Officer, Helen Philips, for accepting our thoughts and advice with a generous and incisive grace.