

# NATURAL ENGLAND BOARD



**Meeting 4**  
**18 April 2007**

Paper No: **NEB P07 13**

Title: **Report on Audit Committee Meeting on 27 March 2007**

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

## **1. Purpose**

- 1.1 The purpose of this paper is to report to the Board the business conducted by the Audit Committee at its meeting held on 27 March 2007.

## **2. Recommendations**

- 2.1 It is recommended that the Board:
- a. note the appended unconfirmed minutes of the Audit Committee's meeting on 27 March 2007 and the contents of this report, and
  - b. determine at a future meeting to take its own in-depth look at the organisation's strategic risk register.

## **3. Introduction**

- 3.1 The fourth meeting of the Audit Committee (and the second since Vesting) took place in London on 27 March. The Committee has moved beyond 'feeling its way', having been strengthened by some high quality National School of Government induction training on 14 March (consolidated by a private meeting of its members after the 27 March formal Committee meeting) and by being better served since the appointment of Mike Doughty as Head of Internal Audit and Dave Webster as Director of Finance and Corporate Services. We now feel better able to provide added value through constructive challenge of staff and suggesting ways in which their internal control mechanisms might be enhanced, always conscious in doing so that they face considerable challenges anyway and what we are reviewing is often, of necessity, work in progress.
- 3.2 In addition to taking stock of the development of the suite of governance documentation at Board and Executive levels and advising on which parts of this documentation should voluntarily be put in the public domain, the Committee reviewed progress on:
- Risk management
  - Internal Audit
  - The assurance processes leading up to the preparation of the Annual Report and Accounts
  - Health and safety

## **4. Risk Management**

- 4.1 Having been concerned at our December meeting that the top-level strategic risk register contained relatively opaque headline risk descriptions, the Committee welcomed the Executive's response in an updated risk register which had a transparent explanation of the various counter-measures being applied to reduce the probability and impact of each risk.
- 4.2 We were comforted to learn the steps being taken to 'embed' risk management in the organisation's normal performance management processes and by the honest and realistic assessment that well thought-through risk-taking and innovation will take time to establish within Natural England's culture at every level. [The Executive is clearly taking steps to shift the middle and junior management perception that Natural England is solely centrally driven, by stressing how much scope there is for initiative to produce desired outcomes in innovative ways within constrained budgets.] This will take time to achieve beyond ELG level, and the Committee will continue to probe to establish that there is an increasingly genuine 'bottom-up' contribution to risk identification, sensible risk-taking and risk management.
- 4.3 In particular we suggested that at an early stage the Executive should overtly (rather than implicitly) establish the organisation's 'risk appetite' against each of the strategic risks. We will return at a future meeting to the concept of distinguishing where the organisation's controls need to be 'tight' – for example, by defining those areas where there can be no variation in practice between regions, or where no delay in agri-environment scheme payments can be tolerated in the early months of Natural England's vulnerable reputation – and where they can be 'looser' to encourage innovation and sensible risk-taking.
- 4.4 We reviewed the items in the Executive's strategic risk register and suggested additional focus on:
- the internal morale and external stakeholder risks associated with the perceived 'winners and losers' in the Corporate Plan financial allocations;
  - the risk of catastrophic IT collapse;
  - the risk of failing to exploit opportunities as well as of facing threats;
  - the risks arising from unfulfilled expectations with regard to Environmental Stewardship (particularly post-ESA);
  - the possibility of exploring the creation of a joint risk register with Defra Shared Services and even IBM.
- We would also take more comfort if the Board as a whole took an in-depth look at the risk register.

## **5. Internal Audit**

- 5.1 We reviewed Internal Audit's draft strategy, its progress against the 2006/7 workplan, its proposed workplan for 2008/9, and steps being taken to strengthen the Internal Audit resource. In discussion, the Committee:
- suggested ways in which the strategic linkage between the Internal Audit's approved terms of reference and its detailed workplans needed to be further developed before the tender exercise for contracted Internal Audit service provision for 2008/9 and beyond;

- expressed some disappointment at slippage against the 2006/7 workplan;
- noted that the 2007/8 workplan had about 15% slack in it to cope with necessary change, and suggested that prime candidates for such flexibility might be reviewing risk management processes in due course, levels of success in establishing the integrated delivery vision which underpins Natural England, and carrying out reality-check audits at regional/team levels;
- noted steps in hand to co-ordinate the NE and NAO workplans to avoid duplicating regions visited;
- suggested the need for Internal Audit to horizon-scan rather than to concentrate investigations solely on areas which were already prominent on management's radar; and
- noted steps in hand to contract Internal Audit services for 2006/7.

5.2 The Committee strongly proposed that, if Internal Audit's choice of workplan was intended to reflect the priorities in the Executive's strategic risk register, it followed that Internal Audit should test the foundations on which it stood by quality-assuring the developing risk management system.

## **6. Preparing the Annual Report and Accounts**

6.1 We were pleased to note from a National Audit Office (NAO) report on their progress in assessing how Natural England was coping with the key audit risks NAO had identified in December that there were no horrors emerging, despite their continuing concern that Defra was failing to sort out all the RDS elements coming to us from the first half-year and that the Shared Services relationship with Natural England was still inadequately settled. NAO does have a concern that Natural England may be insufficiently advanced in planning the preparation of its annual accounts to meet the pre-Recess deadline. Executive Director Finance and Corporate Services explained how his Finance team was being strengthened. The Executive will separately propose to the Board that it delegates for this year its role in approving the accounts to the 18 June Audit Committee, because the July Board meeting is too late, and the Committee will consider whether to hold an interim meeting to review what the accounts might look like in presentational terms.

6.2 The Committee and the NAO were pleased to see two draft detailed questionnaires designed to secure assurances of the ELG, Team Managers and Defra Shared Services that a comprehensive range of internal controls were effectively operating in 2006/7 and to expose any weaknesses. They will provide a robust hierarchy of assurances to sit alongside those provided by the founders for the first half, the Internal Audit annual report and the NAO Management Letter to assist the confident production of the Accounting Officer's Statement of Internal Control, to be incorporated in the Annual Report. We satisfied ourselves that her potential exposure by reason of Defra's encouragement to continue making agri-environment payments beyond the currently authorised funding will quickly reduce as the new ERDP is agreed.

## **7. Health and Safety**

- 7.1 The Committee considered a progress report on setting up new Health and Safety structures for Natural England and statistics on early accident and near miss incidents. We were encouraged by the progress and that Eversheds had been giving senior management some rigorous training on their Health & Safety responsibilities.

Paper No: AC/2/M1

**Draft Unconfirmed Minutes of the Second Natural England Audit Committee Meeting 27 March 2007, 11.30-14.00**

|                       |                     |   |
|-----------------------|---------------------|---|
| <b>Present:</b>       | Christopher Pennell | Chair   |
|                       | David Hill          |   |
|                       | Pam Warhurst        |   |
| <b>In attendance:</b> | Helen Phillips      | Chief Executive                                   |
|                       | Dave Webster        | Executive Director Finance and Corporate Services |
|                       | Adrian Belton       | Executive Director Operations (Items 5&6)         |
|                       | Liz Newton          | Director Risk and Governance                      |
|                       | Helen Dixon         | Director, National Audit Office                   |
|                       | Steve Allen         | Manager, National Audit Office                    |
|                       | Mike Doughty        | Head of Internal Audit                            |
|                       | Terry Towns         | Senior Specialist Health and Safety (Item 5)      |
|                       | Tony Dover          | Senior Specialist Risk (Item 6)                   |
|                       | Jonathan Wray       | Senior Specialist Risk and Governance (Items 7&8) |
|                       | Emily Finnie        | Internal Audit Team Leader (Secretariat)          |
| <b>Apologies:</b>     | Poul Christensen    |   |

**Welcome**

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

On behalf of the Committee the Chair congratulated Liz Newton on her appointment to Regional Director North West and Mike Doughty on his appointment to Head of Internal Audit.

The following interests were declared: Christopher Pennell was a member of the English Nature Council until Vesting.

- 1. Minutes of the 1st Meeting of the Audit Committee held on 4 December 2006 (AC/1/M1)**
  - 1.1 The Committee **confirmed** the minutes of the first meeting of the Audit Committee without amendment.
  
- 2. Matters Arising (AC/2/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 Dave Webster reported progress with the recruitment of a fifth (external) member of the Committee. The Committee noted that acceptance of the position was awaited from a candidate interviewed recently by the Chair and Dave Webster. Dave Webster would notify members as soon as the appointment had been confirmed. **(Action DW)**
- 2.3 Helen Dixon confirmed that NAO was satisfied that there was no absolute requirement for separate accounts for the founding bodies for 2006/07 and that the pragmatic solution was for their accounts to be incorporated into the final Natural England accounts for 2006/07.
- 2.4 The Chair reported that he and members of the Audit Committee had received excellent induction training from the National School of Government on 20 February 2007. They would be having follow up discussions to consolidate this training after this Audit Committee meeting.

### **3. Internal Audit Report (AC/2/P1)**

- 3.1 Mike Doughty introduced the internal audit report that provided an update on the provision of internal audit services and activity in Natural England.

#### **Internal Audit Strategy (Annex1)**

- 3.2 In reviewing the suggested Internal Audit Strategy the Committee:
  - 3.2.1 noted the Strategy set out the proposed approach to internal audit as defined in the Terms of Reference and that it included the development of the wider assurance co-ordination role for the organisation;
  - 3.2.2 noted the size of the in-house internal audit team supplemented by the external provision of internal audit services;
  - 3.2.3 stressed the importance of a robust process for the internal audit team's relationship with the regional agenda, and noted that this would be covered by arrangements for risk management and the regions' involvement in signing off the scopes for internal audit reviews;
  - 3.2.4 advised that extra training and development may be needed in the organisation on the internal control agenda;
  - 3.2.5 advised that the organisation needed to distinguish between areas where controls needed to be 'tight' and others where there could be greater freedom for innovation, and noted that the Executive Leadership Group was discussing empowerment and delegation.
- 3.3 The Committee concluded that the Strategy was not yet sufficiently developed and recommended that before the contract was let for 2008/09 and beyond, the Strategy should be developed to include additional areas such as attitude to risk, strategic linkages between the Internal Audit Terms of Reference and detailed work plans and relationships with the external contract provider. The Chair would discuss this with Mike Doughty **(Action: CP and MD)**

#### **Internal Audit Progress Report for 2006/07 (Annex 2)**

- 3.4 The Committee reviewed the progress report for 2006/07 and noted action completed against planned reviews identified at the December meeting. In discussion the Committee:
- 3.4.1 noted with disappointment some slippage in the work plan due to scheduling and resourcing issues;
  - 3.4.2 re-iterated its advice that there should be a review of Genesis before Natural England took over responsibility from Defra;
  - 3.4.3 noted that discussions with the Internal Audit section of the Rural Payments Agency had resulted in a Service Level Agreement between the two teams setting out the working relationships and assurances each organisation could take from the work of each other;
  - 3.4.4 while noting that the quarterly performance reviews were designed to provide opportunities for networking and disseminating best practice, advised that regional internal audit reviews should also contribute to this;
  - 3.4.5 endorsed the Chief Executive's view that internal audit reports would not come to the Committee until actions were agreed by the sponsoring Executive Director and the Executive Board had reviewed the management action plan;
  - 3.4.6 noted in future this report would include information on the implementation of audit recommendations (there were none to report on for this meeting).

#### **Internal Audit Programme for 2007/08 (Annex 3)**

- 3.5 The Committee reviewed and **approved** the proposed Internal Audit programme for 2007/08 subject to the following points raised in discussion. The Committee:
- 3.5.1 noted the core programme was designed to be delivered by the contractor with spare capacity in the contract to add some extra reviews, and there would also, once appointed, be resource available from the in house auditor;
  - 3.5.2 noted that while the risk based programme was designed to be flexible, it was not envisaged that the broad areas for review would change significantly, but the scope for each review could change up to being signed off by the Executive Director;
  - 3.5.3 noted the extra benefits to be obtained from Natural England conducting a review of the BIG Lottery Green Spaces grants scheme;
  - 3.5.4 stressed the importance of an early review of organisational reputation;
  - 3.5.5 recommended it was good practice to include regional reviews in the programme and noted that there were steps in hand to co-ordinate Natural England and NAO work plans to avoid duplication of regional reviews;
  - 3.5.6 reviewed coverage of the corporate risks and noted that while risk 3 (failure to achieve the integrated delivery vision that underpins the creation of Natural England) was missing from the work plan, it was premature to include until the Integrated Service Delivery project was underway but would then be important to review;

- 3.5.7 recommended that a prime candidate for an additional review would be the risk management process (particularly since the choice of areas for audit was significantly based on this), and that there could also be benefit from internal audit reviewing areas not identified in the corporate risk register because they were areas not already prominent on management's radar;
- 3.5.8 noted that NAO viewed the programme as providing reasonable and comprehensive coverage but would wish to revisit the work plan informed by the 2006/07 audit once it was completed.

#### **Update on Internal Audit Resources**

- 3.6 The Committee noted and **endorsed** the update on resources including contract arrangements for 2007/08. The Chair asked Mike Doughty to brief him on the contract for 2007/08 outside the meeting. **(Action: MD)**

#### **4. External Audit: Annual Report and Accounts 2006/07 Interim Progress Report (AC/1/P2)**

- 4.1 Helen Dixon introduced the interim progress report that presented commentary on each of the areas of audit risk identified in the NAO audit strategy considered at the December Audit Committee meeting.
- 4.2 NAO reported three main findings and the Committee:
  - 4.2.1 noted that increased priority would need to be given to the production of the final Annual Report and Accounts if the pre-Recess timetable was not to be put at risk, but was reassured by Dave Webster's confirmation that there were now sufficient resources available within the Finance team that would be redeployed to ensure that the deliverable items and milestones to be agreed with NAO were achieved.
  - 4.2.2 noted key areas on which Natural England was dependent on Defra for a satisfactory resolution;
  - 4.2.3 noted the need to show how use of Genesis should be accounted for in the Annual Accounts.
- 4.3 In reviewing the risk areas the Committee welcomed the helpful report and in discussion:
  - 4.3.1 had hoped that the RDS elements of the accounts would have been resolved by now but noted that this was on-going (A line would be drawn after the 2006/07 Statement on Internal Control was signed.) NAO was confident that it could provide audit assurance because the key risk was Genesis, and that had been held back from the transfer to Natural England at Vesting.
  - 4.3.2 expressed concern that while the arrangements with DFSSD were in place they were not yet formalised through service level agreements for each service being provided.

- 4.4 The Committee noted that NAO would continue to report findings as it progressed its work. Dave Webster would explore with the Chair whether it might be necessary to hold an interim Audit Committee meeting to review the accounts, particularly their presentation, before the next meeting on 18 June. **(Action DW and CP)**

## **5. Implementation of Health and Safety Policy across Natural England (AC/2/P3)**

- 5.1 Adrian Belton introduced the progress report. The Committee supported Natural England's aspiration to be an upper quartile organisation for health and safety and welcomed progress made with publishing and implementing health and safety policy in spite of capacity problems pending recruitment to vacancies.
- 5.2 In discussion the Committee;
- 5.2.1 noted a number of themes emerging including lone working, stress associated with further changes in the organisation, delivery through third parties and inherent risks on National Nature Reserves and other sites;
- 5.2.2 noted the accident and near-miss statistics and arrangements for accident reporting, and advised that under-reporting was likely to be an issue;
- 5.2.3 stressed the importance of promulgating lessons learned with priority to be given to others in a similar position, and was reassured to note that this was picked up both in quarterly performance reviews and by the Occupational Health and Safety Team.
- 5.2.4 noted that, with policies in place, the Occupational Health and Safety Team's emphasis was now on ensuring clarity on procedures;
- 5.2.5 recognised that work on risk assessments for Natural England was a huge job. Those inherited from the founding bodies were adequate and fit for purpose but there was much work to be done to ensure joining together and commonality of purpose.
- 5.3 In conclusion the Committee was encouraged by progress and that senior management had been receiving training on their health and safety responsibilities.

## **6. Risk Management (AC/2/P4)**

- 6.1 Adrian Belton introduced the paper, which, in response to the Committee's concerns at its last meeting, reported progress on embedding risk management and provided an opportunity to share an understanding of the organisation's key risks and progress on actions to mitigate them.
- 6.2 The Committee;
- 6.2.1 found it helpful to have information on counter-measures for the headline risks;

- 6.2.2 noted progress against NAO's guidance for self-assessment on progress with embedding risk management;
- 6.2.3 expressed particular interest in how Natural England could assess whether its culture supported well thought through risk taking and innovation and how long it might take to embed risk management in normal management processes. While risk management was explicit in quarterly reviews, another perspective was provided through the transition programme's impact on the Executive Leadership Group's empowerment discussions and the impact on region and area teams' freedoms.
- 6.3 The Committee reviewed the Natural England top-level strategic risk register and:
  - 6.3.1 was reassured that management was very active in relation to risk 2 'Failure to deliver scheme management to time and standard' noting that at any time of year there would be a different set of actions to manage this risk. Members noted there would be a workshop at the next Board meeting that would provide the opportunity to cover schemes in more detail;
  - 6.3.2 advised that funding issues in relation to the 2007/08 corporate plan would need to be handled carefully because of perceptions about 'winners' and 'losers', and received an update from the Chief Executive about the alignment of resources with priorities and measures in hand to manage the risks involved both internally and with external stakeholders;
  - 6.3.3 advised that the health and safety risk should be captured in proactive, rather than reactive language ie with reference to an upper quartile organisation rather than statutory responsibilities;
  - 6.3.4 suggested additional focus on the risk of a catastrophic IT collapse, and the risk of failing to exploit opportunities as well as facing threats;
  - 6.3.5 advised that there should be an exploration of the scope for developing shared risk registers with Defra and IBM for shared services; **(Action DW and TD)**
  - 6.3.6 advised that the Executive should state the organisation's risk appetite against each of the strategic risks and requested an opportunity to discuss risk appetite at a future meeting. **(Action AB and TD)**
- 6.4 In conclusion the Committee welcomed progress on embedding risk management into the organisation since the last meeting but recognised there was still much to do. The Committee advised that the Board should be invited to review the strategic risk register at a future meeting. **(Action: CP and HP)**

## **7. 2006/07 Statement on Internal Control Assurance Process (AC/2/P5)**

- 7.1 Dave Webster introduced the paper that set out the proposed additional new assurance process that would be adopted to help with development of the 2006/07 Statement on Internal Control.
- 7.2 The Committee warmly welcomed the controls questionnaire noting that the internal questionnaire would be sent to the Executive Leadership Group and

Heads of Teams and that the second questionnaire would be sent to Defra Shared Services.

- 7.3 In discussion the Committee:
- 7.3.1 advised that the questions should be reviewed by Dave Webster before the questionnaire was issued because there were some questions where comment would be required unless the respondent entirely (rather than partly) agreed that the control was operating correctly ; these should be clearly identified;**(Action DW)**
  - 7.3.2 noted NAO confirmed that such questionnaires were good practice and, along with its findings and assurance from Internal Audit, would support the Statement on Internal Control, but noted NAO advised that some quality assurance of the returns would be necessary;
  - 7.3.3 was reassured that this was a tried and tested model;
  - 7.3.4 recognised that the results of the questionnaire would be a valuable resource for targeting development and training needs, providing a baseline for monitoring progress and for influencing the scope of internal audit reviews.
- 7.4 The Committee noted it would have an opportunity to consider and comment on the Statement on Internal Control at its June meeting.

## **8. Update on Status of Governance Framework (AC/2/P6)**

- 8.1 Dave Webster introduced the paper on the status of the governance framework.
- 8.2 The Committee took comfort from the wide range of governance documents and the amount of good work leading to their production. In supporting Natural England's objective of becoming an exemplar on corporate governance, the Committee **agreed** this should be demonstrated by making the documents available on the internal intranet as a 'virtual governance manual'. **(Action DW and JW)**
- 8.3 The Committee stressed the importance of updating the corporate governance documents regularly and advised that in addition to the list of suggestions for publication on the external website, it would be helpful to include the corporate plan, annual report and accounts, risk management policy and a list of memoranda of understanding signed between Natural England and other organisations. **(Action DW and JW)**

## **9. ELS and HLS Contingency Arrangements**

- 9.1 Dave Webster gave an update following discussion at the last meeting. The Committee noted that the impending announcement on the ERDP removed the requirement for an immediate exchange of Accounting Officer letters.

## **10. Cases of Fraud of Presumptive Fraud**

- 10.1 The Committee noted that this was a standard agenda item. Dave Webster reported that there were no cases to report.

## **11. Review of Meeting and Forward Look (AC/2/P7)**

- 11.1 The Committee reviewed the meeting, which was considered an improvement on its first meeting assisted by good papers and improvement in members' knowledge following their training. The Chief Executive considered it to have been an excellent meeting with a good balance between challenge and advice.
- 11.2 The Committee reminded itself of its programme of future business in Annex1 and noted that additional time would be needed at the June meeting to give proper consideration to the Annual Report and Accounts. It had not been possible to rearrange the date of the July Board meeting to give the full Board the opportunity to agree the Annual Report and Accounts, and at its next meeting the Board would be asked to agree that the Audit Committee undertook this task on its behalf. **(Action CP and DW)**
- 11.3 The Committee had accepted that its December meeting might take place on the morning before the following day's Board meeting so long as the Committee's time was not 'crowded' by early informal Board activities on 11 December. **(Action: DW)**

## **12. Any other Business**

- 12.1 The Committee noted that HM Treasury had now published the final version of the *Audit Committee Handbook* and that they would be sent copies shortly. **(Action MD)**

## Action Points

### Second Meeting of the Natural England Audit Committee – 27 March 2007

| No | Min ref | Action  | Responsibility                         | Action taken |
|----|---------|---|--|--------------|
| 1  | 2.2     | Send out note to Audit Committee members once appointment of fifth member is confirmed.   | Dave Webster                           |              |
| 2  | 3.6     | Brief the Chair on the contract for 2007/08.  | Mike Doughty                           |              |
| 3  | 4.4     | Review the need for an interim Audit Committee meeting to review the Annual Accounts before 18 June.  | Dave Webster and Christopher Pennell   |              |
| 4  | 6.3.5   | Explore of the scope for developing shared risk registers with Defra and IBM for shared services  | Dave Webster and Tony Dover            |              |
| 5  | 6.3.6   | Provide a paper on risk appetite for a future meeting.  | Adrian Belton and Tony Dover           |              |
| 6  | 6.4     | The Board should be invited to review the strategic risk register at a future meeting   | Helen Phillips and Christopher Pennell |              |
| 7  | 7.3.1   | Review the internal controls questionnaire before issue.  | Dave Webster                           |              |
| 8  | 8.2     | Demonstrate corporate governance through a “virtual governance manual” on Natural England’s intranet  | Dave Webster and Jonathan Wray         |              |
| 9  | 8.3     | Update the corporate governance documents to include the corporate plan, annual report and accounts and a list of memorandum of understanding signed between Natural England and other organisations. | Dave Webster and Jonathan Wray         |              |
| 9  | 11.2    | Seek Board approval of the handling of the Annual Report and Accounts for 2006/07.  | Dave Webster and Christopher Pennell   |              |
| 10 | 11.3    | Manage scheduling of Audit Committee meeting on 11 December 2007 with any Board Meeting activities.   | Dave Webster                           |              |
| 11 | 12.1    | Send Members copies of the final <i>Audit Committee Handbook</i> .  | Mike Doughty                           |              |

