

**Minutes of the MHS Audit Committee held on 22 May 2007**

**Summary**

Board members are asked to **note** the minutes of the MHS Audit Committee held on 22 May 2007. **No action** is required.

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MHS Audit Committee Meeting  
Tuesday, 22 May 2007  
London

**Attendees:**

Committee Members:

Deryk Mead, Chair  
Ian Reynolds  
Bill McLaughlin

Officials:

Steve McGrath, MHS  
Kathryn Davies, MHS  
Mike Doré, MHS  
Freedom Mpande, MHS Internal Audit  
Peter Clarke, NAO

**1 Apologies for absence**

- 1.1 Apologies were received from Claire Rollo, NAO, John Cragg, FSA and Kevin Goddard, MHS.

**2 Minutes from previous meeting – 29 March 2007 – AC (07) 20**

- 2.1 Point 5.4 should state that the issue of approval of the MHS budget should be considered by the “roles and relationship review”.
- 2.2 Point 10.2 should have identified an action regarding the proposal that the audit burden should be included in the FSA’s review of the delivery of official controls. Ian Reynolds confirmed that he had raised the issue with Geoff Tierney (Programme Manager for the review).
- 2.3 Point 12.2, it was also agreed that draft Audit Committee minutes should be circulated to the MHS Board. This would provide context for the Chair of the Audit Committee’s report to the MHS Board.

**Action: Kevin Goddard**

- 2.4 Subject to the items noted above, the minutes of the previous meeting were agreed.

**3 Action points arising from previous meeting - AC (07) 21**

- 3.1 Point 32 - Deryk Mead expressed concern regarding the number of recommendations still outstanding, particularly those relating to risk management. Kathryn Davies stated that a review of risk management was underway, which will pick up these outstanding issues. Bill McLaughlin

highlighted a high risk recommendation not yet cleared, referring to the Audit of the H123 Project. He advised that work to clear issues should be prioritised by risk and requested that progress on outstanding recommendations should be reported based on priority in future.

**Action: Kevin Goddard**

#### **4 Draft Annual Report and Accounts 2006/07 – AC (07) 22**

- 4.1 Kathryn Davies presented this paper. In terms of the process, the drafts were provided for the NAO to commence its audit three weeks after the year-end as expected. Subsequently, the drafts and a True and Fair View Paper were sent to Audit Committee members for early review. The NAO completed its audit within three weeks and the Accounts were being finalised prior to the Audit Committee Meeting.
- 4.2 The drafts included a Management Commentary, incorporating Performance against Corporate Objectives and Financial Performance, a Statement on Internal Control, Corporate Governance and an updated Remuneration Report. An explanation of the year-to-year variances was also provided, which demonstrated that due process had been undertaken to reflect a true and fair view of the state of affairs of the MHS.
- 4.3 The financial targets had been met for the year, with net operating cost showing a £0.9m favourable variance and cash showing £1.9m favourable to budget. Comparing the year-to-year results, Net Operating Cost had increased by £1.7m. Income had increased due mainly to additional Government work, particularly Defra but offset by lower activity for the FSA and RPA. Expenditure had also increased, due mainly to additional contractor costs and pay inflation but offset by reduced overtime and other savings. The FRS17 pension disclosures and the associated effect on credit cost of capital had produced a decrease in net operating cost compared with the previous year, but the LGPS liability had increased by £19.4m to £46.7m. This large movement provided the main reason for an increase in net liabilities, supplemented by an increase in net current assets, although fixed assets reduced.
- 4.4 Bill McLaughlin asked if the actuarial figures had been challenged and advised that the actuary should be held accountable for the results. Mike Dore explained that the results had been investigated, with explanatory information and reports being made available from the actuary, LPFA and Treasury. A change in the Treasury directive for a less preferential net discount rate to be used this year, 2.2% from 2.8%, together with an improvement in life expectancy, resulted in a large increase in pension liabilities. However, it was noted that the pension liability had swung significantly over the last three years due to the use of different criteria by the actuary.
- 4.5 Deryk Mead raised a concern that, whilst the use of the term “Administration Costs” in the Accounts was technically correct, there was a danger that the public could misunderstand this as unnecessary MHS overhead costs. Deryk suggested that the presentation could be improved and consideration should be given to including a more detailed explanation of the term in the accounts.

- 4.6 Peter Clarke suggested an improved format to the Annual Report, which will be implemented.
- 4.7 Ian Reynolds wanted assurance and accountability from the FSA's Director of Finance and asked if the Accounts had been signed off by him. Kathryn Davies replied that Steve McGrath held this accountability and had been assured by the MHS Director of Finance and the Senior Management Team during the approval process. Allan Hutton had received the Accounts along with the other Audit Committee papers but no comments had been sent as yet. [Post-meeting note: Allan Hutton has subsequently responded that, after obtaining answers to some questions, he has no observations to make on the Accounts. He has taken assurance from Steve McGrath and his Finance Team that the Accounts are correct and suitable for consolidation.]
- 4.8 Bill McLaughlin asked if it was necessary for the document to be of such length. Steve McGrath inherited the present format in order to meet the timetable but would prefer a separate Annual Report and Accounts. Peter Clarke emphasised the statutory requirements for Parliament. Steve McGrath accepted this and will aim next year for a minimum requirement ARA for Parliament and a separate report for the public/stakeholders, which would be more informative as a public relations document.
- 4.9 Minor points of presentation in the Accounts and the Remuneration Report will be amended.
- 4.10 From next year, Steve McGrath suggested that the Audit Committee should give its recommendation that the MHS Board meets to approve the Annual Report and Accounts prior to him signing the Accounts.

**Action: Deryk Mead**

## **5 Emerging findings from NAO audit 2006/07/ISA 260 – AC (07) 23**

- 5.1 Peter Clarke presented the paper highlighting the results of the NAO audit, including a combined ISA 260 Report and Management Letter for the first time, enhancing faster closure.
- 5.2 He stated that the NAO will recommend an unqualified opinion regarding the Report and Accounts for the subsequent sign-off of the Audit Certificate. This opinion resulted from the results of its audit, including a review of the True and Fair View report, the Remuneration Report and the information in the Annual Report being consistent with the Accounts.
- 5.3 The Management Letter contained only three minor recommendations, all of which have been accepted. In addition, financial adjustments had been incorporated in the Accounts.
- 5.4 A draft Letter of Representation was available for management to consider. Steve McGrath asked whether there may be an opportunity to change the accountability for next year, but this was felt to be unlikely. However, it was suggested that he may wish to obtain a sign-off from the MHS and FSA Directors of Finance in future.

- 5.5 Peter Clarke outlined the process for sign-off and approval from this point.
- 5.6 He expressed his appreciation to the MHS for its work in providing the NAO team with the appropriate information in a timely manner.
- 5.7 Ian Reynolds requested that this NAO Report be sent to the MHS Board as an inter-sessional paper to reinforce the Board's awareness of governance.

**Action: Kevin Goddard**

He felt that the Report and Accounts were robust and of good quality to facilitate a fast closure.

- 5.8 The Audit Committee agreed the audit findings presented by the NAO and confirmed that the information contained in the Annual Report and Accounts gave a true and fair view of the state of affairs of the MHS. It also wished to thank all participants for the preparation of the Annual Report and Accounts.

## **6 MHS Internal Audit Annual Report for 2006/07 – AC (07) 24**

- 6.1 Freedom Mpande highlighted the contents of the Annual Report:-

- He confirmed that, based on internal audit's work during the year, in his opinion the MHS has a generally adequate and effective framework of risk management, control and governance processes, which gave reasonable assurance that the business objectives will be achieved.
- In particular, he drew attention to the results of the audit work undertaken for official controls and financial, IT, HR and corporate governance systems and processes. In addition, a number of external reviews of MHS activities had been completed during the year.
- With regard to support systems and processes, most of the audits were rated as adequate or good. However, he brought attention to the weak opinion given in the audit report on the audit of Overtime Payments, which has resulted in a reassessment of this area to a high risk category. Overall, there were 10 high priority recommendations out of the 38 accepted.
- Audits of MHS service delivery in plants resulted in predominantly adequate and good opinions.

- 6.2 Ian Reynolds felt that a framework of prioritising was required, relating the percentage of establishments audited to the total number of establishments, and questioned the process of choosing the establishments included in the audit programme. He felt that although the Report confirmed what had been done, it did not explain why. Freedom explained that there was a separate process under which risks associated with individual establishments and hence the frequency of cyclical audits were determined. Freedom undertook to make this clearer in future reports.

**Action: Freedom Mpande**

6.3 Bill McLaughlin was concerned about the potential £1.4m problem arising from the weaknesses in the overtime payments process, and enquired whether any recommendations had been implemented. Freedom Mpande confirmed that this will be followed up during the next few months including a return to plants where the problem had been identified, supplemented by additional sample audit checks during the year. Progress on this issue would be reported back to the next Audit Committee meeting.

**Action: Freedom Mpande**

6.4 Bill McLaughlin suggested that a structuring of 2007/08 audit plans was required as a result of the findings from this year. This included changing the emphasis of audits from official controls to administrative key controls and providing greater attention to finance rather than administration. Progress on this issue would be reported back to the next Audit Committee meeting.

**Action: Freedom Mpande**

6.5 The Committee accepted the Report.

## **7 Level 1 Risk Register – AC (07) 26**

7.1 Kathryn Davies informed the Committee that the risk register had been revised, following a realignment of corporate objectives. As a result, the following main changes and comments apply:

- Risk 13 – Now considered to be the top risk, bearing the highest risk rating. Consultancy assistance for the MHS Transformation Project has been approved by the FSA.
- Risk 2 – Reduced likelihood, therefore risk rating reduced from 3 to 2.
- Risk 6 – Reduced likelihood, therefore reduced to 2.
- Risk 3 – Consultancy support has been received from the FSA.
- Risk 14 – IIP re-accreditation has been delayed to September 2007.
- Risk 16 – MHS is subject to cross-Government contingency planning.

7.2 In response to Bill McLaughlin's question regarding regularity of risk register review, Kathryn Davies replied that it was reviewed monthly by the MHS Senior Management Team.

## **8 Any Other Business**

8.1 Deryk Mead expressed his and the Committee's thanks to Bill McLaughlin for his service as a member of the Committee over the years and was particularly appreciative for his advice. An advertisement was in the process of being prepared for his successor.

## **9 Date of Next Meeting**

9.1 The next meeting is due to be held on **17 September 2007**, venue to be confirmed later.

