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## **JOINT NATURE CONSERVATION COMMITTEE**

### **THE JNCC AUDIT AND RISK MANAGEMENT COMMITTEE**

#### **Paper by Tracey Quince**

#### **1. Introduction**

- 1.1 At its June 2004 meeting the Joint Committee agreed a corporate governance model for the JNCC once the company limited by guarantee (CLG) is established. This included formal delegation by the Joint Committee to the company of the responsibility of setting up an Audit Committee as a sub-Committee of the Company Board. The scope of the Audit Committee would extend to all of JNCC's business whether delegated to the company or reserved by Committee and it would comprise at least two 'independent' non-executives. It was agreed that the Committee Chair will have direct access to the Joint Committee for concerns regarding the company.
- 1.2 The Audit and Resources Sub-Group has been consulted on the proposed principles and arrangements outlined in this paper and endorsed the proposal to extend the scope of the sub-Committee to incorporate risk management. The Sub-Committee would therefore be referred to as the Audit and Risk Management Committee.
- 1.3 It is proposed to establish the Audit and Risk Management Committee in the autumn to enable the new arrangements being established for the organisation to be scrutinised effectively at Committee level. The Audit and Risk Management Committee will run in parallel with country agency Audit and Risk Management Committees until the new arrangements come into force formally in 2005. One of the first tasks of the Audit and Risk Management Committee will be to appoint internal auditors. It is envisaged that a contract for the provision of internal audit will be let by December. The Audit and Risk Management Committee will therefore be asked at its first meeting to agree the specification for provision of the services and eventually to formally award the contract.

#### **2. Role of the Audit and Risk Management Committee**

- 2.1 The essence of the function of the Audit and Risk management Committee in the JNCC will be to support the company board, and through them the Joint Committee, by monitoring and reviewing both the risk, control and governance processes which have been established in the organisation, and the associated assurance processes.

- 2.2 The Audit and Risk Management Committee will be the means by which the company board, and through them the Joint Committee, are provided with assurance about the conduct of the affairs of the organisation and further assurance about the robustness of the assurance mechanisms that are in place. The Audit and Risk Management Committee will also be a useful mechanism for ensuring appropriate high level information on risk and control is brought to the Board's attention to assist it in identifying priorities for action.
- 2.3 The Audit and Risk management Committee should carry out its work by reviewing and challenging the assurances, the way in which these assurances are developed, and the management priorities and approaches on which the assurances are premised. Whilst there are a range of detailed responsibilities which might be assigned to the Audit and Risk Management Committee, it is not its task to be a substitute for the executive function in the management of internal audit, risk management, corporate governance, control and risk assessment, or any other review or assurance function. However, the Audit and Risk Management Committee should offer opinions or recommendations on the way in which such management is conducted.
- 2.4 Draft terms of reference can be found at Annex 1. However, these are not exhaustive and further guidance on the key questions which the Audit and Risk Management Committee might ask on the issues which it is required to consider can be found at Annex 2.

**3. Audit and Risk Management Committee relationship with the company board, the Joint Committee and agency Audit and Risk Management Committees.**

- 3.1 In line with common practice it is intended that the Audit and Risk Management Committee will formally report back to the company board in order that the whole board may consider the assurances and advice provided by the Audit and Risk Management Committee.
- 3.2 By delegating responsibility for establishing the Audit and Risk Management Committee to the company the Joint Committee will seek to gain much of its assurance from the company. However, it is intended that the Audit and Risk management Committee should also report directly to the Committee to enable the Committee to gain additional assurance independently from the company.
- 3.3 Finally, because of the status of the Joint Committee as a Committee of the country agencies and that of the country agency Chief Executives as the Joint Accounting Officers of the JNCC it is also considered necessary for the Audit and Risk Management Committee to provide its reports to the Audit and Risk Management Committees of the agencies to enable them to provide the necessary assurances to their own Councils/ Board. Additional means of providing assurance, such as providing access to internal audit reports and external audit communications will also be required.

#### **4. Audit and Risk Management Committee competencies**

- 4.1 The Audit and Risk Management Committee will require a range of competencies to allow it to be effective in its functions. These competencies will include understanding the government environment and accountability structures; understanding of the function of the organisation; financial/accountancy skills; and management skills. A more detailed listing is at Annex 3.
- 4.2 It will also be important that those appointed to the Audit and Risk Management Committee are provided with suitable induction training to allow them to understand the organisation and effectively contribute to the achievement of the Committee's terms of reference. It is intended to provide suitable training for members as soon as possible.

#### **5. Composition of the Audit and Risk Management Committee**

- 5.1 The role of the Audit and Risk management Committee is achieved through provision of an independent perspective and a process of constructive challenge. The Committee should therefore have no authority in its own right over the operations of the organisation or those bodies which conduct audit and assurance, including internal audit. Membership of the Audit and Risk Management Committee should therefore be drawn from those charged with governance in a non-executive capacity who also have no other interests that could impinge on their objectivity. There should also be an element of common membership of the Audit and Risk Management Committee and company board. This enables the Audit and Risk Management Committee to know and understand the board's priorities and ensures that Audit and Risk Management Committee views are properly represented in board discussions, including those concerning reports received from the Audit and Risk Management Committee. The Chair of the Committee should not be the person to whom the Committee is giving advice or the Chair of any other committees to avoid potential conflicts of interest. It is proposed that four internal members are selected, one of whom should be appointed as the Chair.
- 5.2 The objectivity of the advice provided by the Audit and Risk Management Committee can be enhanced if the Audit and Risk Management Committee includes an independent external member. This also provides the opportunity to fill any gaps in the competencies of the Committee. For these reasons it is proposed to seek one external member once internal members have been identified.

#### **6. Role of executives**

- 6.1 The role of executives at the Audit and Risk Management Committee is to provide the specialist knowledge needed to ensure that discussions are appropriately and adequately informed. It is proposed that the Managing Director as analogous to the Accounting Officer, the Director of Resources and External Affairs and the company secretary should normally attend meetings. However,

executive managers attending the Audit and Risk Management Committee (other than the Managing Director as analogous to the Accounting Officer) should ideally be rotated on an appropriate cycle (three years is generally appropriate) to provide for objectivity in the long term and to avoid the development of any apparent 'right' of a particular executive interest to be represented on the Audit and Risk Management Committee. Other executives may be invited to attend meetings for a particular item of business, or even to meet from time to time with only 'full members' of the Committee present to facilitate open discussion about a particular issue. The company board/Audit and Risk Management Committee link is also strengthened if the board minuting secretary also acts as the Audit and Risk Management Committee minuting secretary.

- 6.2 Additionally because of the inter-relationship of the JNCC, the company and the country agencies, representatives from the country agencies (beyond Committee members) may wish to attend Committee as observers to gain assurance on behalf of their agency. However, their formal membership of the Committee could give rise to a conflict of interest as the Committee's primary responsibility is to the organisation it serves not the sponsoring body and is therefore not recommended.

## **7. Audit access to the Audit and Risk Management Committee**

- 7.1 Internal and external audit representatives normally would be expected to attend meetings to provide specialist knowledge and opinion to the Audit and Risk Management Committee.
- 7.2 Additionally both the Head of Internal Audit and the external audit representative should have free access to the chair of the Audit and Risk Management Committee in order to raise any concerns they might have. These might include any concerns about the way in which either the planning of their work is being subjected to influence by management or the way in which the results of their work is being handled by management. In addition internal auditors will have escalation procedures for addressing weaknesses which they have identified and which they seek to have corrected in order to allow them to give assurance that risks are appropriately controlled and managed.

## **8. Meetings of the Audit and Risk Management Committee**

- 8.1 It is proposed that three or four meetings a year should be sufficient for the JNCC's purposes. Much of the work of the Audit and Risk Management Committee can be related to particular times of the year. For example consideration of proposed internal audit plans should be carried out before the beginning of the financial year, whilst consideration of an audit opinion as a contribution to preparing the Statement of Internal Control can only be carried out once the audit opinion has been drafted which is likely to be some time after the end of the financial year. It is envisaged that the Audit and Risk Management Committee will be up and running by mid November and should meet shortly after to formally appoint the internal auditors. The first timetabled meeting should take place in December/January in order to undertake the winter meeting agenda.

**DRAFT TERMS OF REFERENCE FOR AN AUDIT AND RISK MANAGEMENT COMMITTEE**

1. The company board has established an Audit and Risk Management Committee to support them in their responsibilities for issues of risk, control and governance and associated assurance.

**2. Role**

2.1 The Audit and Risk Management Committee is an advisory Committee established to:

- i. promote a climate of financial discipline and internal control to reduce the opportunity for financial or other mismanagement;
- ii. advise the Accounting Officer on priorities for the Internal Audit team including its long term plan annual work programme;
- iii. support and advise the Accounting Officer on all internal and external audit matters;
- iv. give advice to the Accounting Officer on the adequacy of risk management policy and on the implications of assurances provided in respect of risk and control in the organisation;
- v. promote the understanding of Internal Audit's role and value within the JNCC.

**3. Membership**

3.1 The members of the Audit and Risk Management Committee are:

- i. Non-executive Board members: *List those who are appointed to the Audit and Risk Management Committee;*
- ii. External members: *List those who are appointed to the Audit and Risk Management Committee;*
- iii. Other members: *List those who are appointed to the Audit and Risk Management Committee (indicate the date of appointment and when the appointment is due to end/become eligible for renewal);*
- iv. The Audit Committee will be chaired by.....(tbc).....;
- v. The Audit Committee will be provided with a secretariat function by.....(tbc).....;

#### **4. Meetings**

- i. the Audit and Risk Management Committee will meet at least three times a year. The Chair of the Audit Committee may convene additional meetings as they deem necessary;
- ii. a minimum of three members of the Audit and Risk Management Committee will be present for the meeting to be deemed quorate;
- iii. Audit and Risk Management Committee meetings will normally be attended by the Accounting Officer, the Director of Resources & External Affairs, the Head of Internal Audit and a representative of external audit;
- iv. the Audit and Risk Management Committee may ask any other officials of the organisation to attend to assist it with its discussions on any particular matter;
- v. the Audit and Risk Management Committee may ask any or all of those who normally attend but who are not members to withdraw to facilitate open and frank discussion of particular matters;
- vi. the Accounting Officer or company board may ask the Audit and Risk Management Committee to convene further meetings to discuss particular issues on which they would like the Committee's advice.

#### **5. Access**

- 5.1 The Head of Internal Audit and the representative of external audit will have free and confidential access to the Chair of the Audit and Risk Management Committee.

#### **6. Reporting**

- 6.1 The Audit and Risk Management Committee will formally report back in writing to the company board after each meeting. Minutes of each meeting will also be circulated to regular attendees.

#### **7. Responsibilities**

- 7.1 The Audit and Risk Management Committee will advise the company board on:
  - i. the strategic processes for risk, control and governance and the Statement of Internal Control;
  - ii. the accounting policies, the accounts, and the annual report of the organisation, including the process for review of the accounts prior to submission for audit, levels of error identified, and management's letter of representation to the external auditors;

- iii. the planned activity and results of both internal and external audit;
- iv. adequacy of management response to issues identified by audit activity, including external audit's management letter;
- v. assurances relating to the corporate governance requirements for the organisation;
- vi. (where appropriate) proposals for tendering for either internal or external audit services.

## **8. Information requirements**

8.1 The Audit and Risk Management Committee will be provided with:

*For each meeting:*

- i. a report summarising any significant changes to the organisation's risk register;
- ii. a progress report from the Head of Internal Audit summarising:
  - work performed (and a comparison with work planned)
  - key issues emerging from Internal Audit work
  - management response to audit recommendations
  - changes to the Periodic Plan
  - any resourcing issues affecting the delivery of Internal Audit objectives;
- iii. a progress report from the external audit representative summarising work done and emerging findings.

*As appropriate:*

- i. proposals for the terms of reference of internal audit;
- ii. the internal audit strategy;
- iii. the Head of Internal Audit's annual opinion and report;
- iv. quality assurance reports on the internal audit function;
- v. the draft accounts of the organisation;
- vi. the draft Statement of Internal Control;
- vii. a report on any changes to accounting policies;
- viii. external audit's management letter;
- ix. a report on any proposals to tender for audit functions;
- x. a report on co-operation between internal and external Audit.

**KEY QUESTIONS WHICH THE AUDIT AND RISK MANAGEMENT COMMITTEE MAY ASK**

1. This list of questions is not intended to be exhaustive or restrictive, nor should it be treated as a tick list substituting for detailed consideration of the issues it raises. This Annex is intended to act as a “prompt” to help the Audit Committee ensure that their work is comprehensive.
  
2. **On the strategic processes for risk, control and governance:**
  - i. How is the organisational risk management culture generated, and is it appropriate?
  - ii. Is there a comprehensive process for identifying and evaluating risk, and for deciding what levels of risk are tolerable?
  - iii. Is the risk register an appropriate reflection of the risks facing the organisation?
  - iv. Is appropriate ownership of risk in place?
  - v. How does management know how effective internal control is?
  - vi. Is risk management carried out in a way that really benefits the organisation or is it treated as a box ticking exercise?
  - vii. Is the organisation as a whole aware of the importance of risk management and of the organisation’s risk priorities?
  - viii. Does the system of internal control provide indicators of things going wrong?
  - ix. How meaningful is the Accounting Officers annual ‘Statement on Internal Control’ and what evidence underpins it?
  - x. Does the Statement on Internal Control appropriately disclose action to deal with material problems?
  - xi. Have the implications of the results of the effectiveness review been discussed at board level?
  
3. **On the planned activity and results of both internal and external audit:**
  - i. Is the internal audit strategy appropriate for delivery of a positive reasonable assurance on the whole of risk, control and governance?
  - ii. Will the periodic audit plan achieve the objectives of the internal audit strategy, and in particular is it adequate to facilitate a positive, reasonable assurance?

- iii. Does internal audit have appropriate resources, including skills, to deliver its objectives?
- iv. Are there any issues arising from management not accepting internal audit recommendations and are agreed internal audit recommendations appropriately actioned?
- v. What assurance is there about the quality of internal audit work?
- vi. Is there appropriate co-operation between the internal and external auditors?

**4. On the accounting policies, the accounts, and the annual report of the organisation:**

- i. Do the accounting policies in place comply with relevant requirements, particularly the Resource Accounting Manual?
- ii. Has there been due process in preparing the accounts and annual report and is that process robust?
- iii. Have the accounts and annual report been subjected to sufficient review by management and by the Accounting Officer and/or Board?
- iv. When new or novel accounting issues arise how is appropriate advice on accounting treatment gained?
- v. Is there an appropriate anti-fraud policy in place and are losses suitably recorded?
- vi. Are suitable processes in place to ensure accurate financial records are kept?
- vii. Are suitable processes in place to ensure fraud is guarded against and regularity and propriety is achieved?
- viii. Does financial control, including the structure of delegations, enable the organisation to achieve its objectives with good value for money?
- ix. Are there any issues likely to lead to qualification of the accounts?
- x. If the accounts have been qualified, is appropriate action being taken to deal with the reason for qualification?
- xi. Are issues raised by the external auditors given appropriate attention?

**5. On the adequacy of management response to issues identified by audit activity:**

- i. Are agreed procedures in place for monitoring progress with the implementation of recommendations?

- ii. If management reject audit recommendations which the auditors stand by, are suitable resolution procedures in place?

**6. On assurances relating to the corporate governance requirements for the organisation:**

- i. Is the range of assurances available sufficient to facilitate the drafting of a meaningful Statement on Internal Control?
- ii. Do those producing the assurances understand fully the scope of the assurance they are being asked to provide and the purpose to which it will be put?
- iii. What mechanisms are in place to ensure the assurances are reliable?
- iv. Are the assurances 'positively' stated (i.e. premised on sufficient relevant evidence to support them)?
- v. Do the assurances draw out material weaknesses or losses which should be addressed?
- vi. Does the Statement on Internal Control realistically reflect the assurances?

**7. On the work of the Audit and Risk Management Committee itself:**

- i. How does the Audit and Risk Management Committee know if it is being effective in achieving its terms of reference and adding value to corporate governance and control systems of the organisation?
- ii. Is the Audit and Risk Management Committee content that it has the appropriate skills mix?
- iii. Is the Audit Committee content with its level of understanding of the purpose and work of the organisation?
- iv. Is the Audit and Risk Management Committee content that it has sufficient time to give proper consideration to its business?
- v. Is the Audit and Risk Management Committee content that it is avoiding any conflict of interest?
- vi. Is there evidence of the Audit and Risk Management Committee's advice having an impact on the organisation?

**AUDIT AND RISK MANAGEMENT COMMITTEE COMPETENCY FRAMEWORK**

**1. All members of the Audit and Risk Management Committee should have, or acquire as soon as possible after appointment:**

- i. understanding of the objectives of the organisation and current significant issues for the organisation;
- ii. understanding of the organisation's structure, including key relationships such as that with a sponsoring department or a major partner;
- iii. understanding of the organisation's culture;
- iv. understanding of any relevant legislation or other rules governing the organisation;
- v. broad understanding of the government environment, particularly accountability structures and current major initiatives.

**2. The Audit Committee should corporately possess:**

- i. knowledge skills/experience (as appropriate and required) in:
  - accounting
  - risk management
  - audit
  - technical or specialist issues pertinent to the organisation's business
  - experience of managing similar sized organisations.
- ii. understanding of the wider relevant environments in which the organisation operates;
- iii. detailed understanding of the government environment and accountability structures.