



**THE NATURAL HISTORY MUSEUM
TRUSTEES' AUDIT & RISK COMMITTEE**

49th Meeting on Thursday 1st July 2010

Present

Sir David Omand in the Chair
Professor Dianne Edwards
Dr Derek Langslow
Mark Richardson (co-opted member)

In Attendance

Dr Michael Dixon (Director)
Neil Greenwood (Director of Finance & Corporate Services)
Jan Day (Acting Head of Risk & Assurance/Committee Secretary)
David Kennedy (Audit Manager, National Audit Office)
Nick Buxton (Partner, PKF)
Martin Burchmore (Partner, Kingston Smith)

Oliver Stocken (Chair of Trustees) was in attendance for item 10 and the remainder of the meeting.

ACTION

- 1 APOLOGIES FOR ABSENCE**
 - 1.1 Keith Lloyd (Director, National Audit Office) sent his apologies.
- 2 DECLARATIONS OF INTEREST**
 - 2.1 There were no declarations of interest.

ACTION

3 MINUTES OF THE MEETING HELD ON THURSDAY 6TH MAY 2010 (PAPER TAC 18/2010)

3.1 The minutes were accepted as a true record of the meeting.

4. MATTERS ARISING FROM THE MINUTES

4.1 There were no matters arising.

5 DIRECTOR'S REPORT (PAPER TAC19/2010)

5.1 The Director presented his paper

5.2 Review of the Administrative Status of Museums – the new government had made a manifesto promise that there would be a review of the administrative status of Museums. This recognised that the current rules on end of year flexibility and access to reserves were not helpful to Museums. The Director alerted the Committee to the fact that a change in status could have financial implications for the NHM.

5.3 It had recently become apparent that the preferred DCMS route to address a change in Museum status was the Public Bodies Reform Bill scheduled for tabling in Parliament in October 2010. Departmental submissions to the Cabinet Office on the Bill were required by 12th July 2010. The Director was concerned that the short timetable may not allow for adequate consultation of DCMS Museums. Please also see Section 10 – Page 7.

6 DIRECTOR OF FINANCE'S REPORT ON THE CURRENT FINANCIAL POSITION AND RESTLESS PLANET UPDATE (PAPER TAC 20 (a), (b) & (c) /2010)

6.1 The Director of Finance & Corporate Services presented his paper.

6 (a) Financial Review for the period April 2009 – March 2010 (Provisional Year End Outturn)

6.2 General Fund - the provisional year end outturn for the General Fund was £2.932m which was £0.477m in excess of the General Fund figure of £2.455m used for the preparation of the balanced budget for 2010/11.

6.3 Self generated \ trading income – it had been a good year for scientific income which had generated a surplus of £2.271 towards overheads. This was significantly above the original budget. Retail remained strong bolstered by high visitor numbers. However, the Director of Finance & Corporate Services observed that the growth rate of retail performance had been slowing down in 2010/11.

6.4 Expenditure - there had been savings from the pay award provision and from energy costs. The Museum had moved from an OGC energy fixed rate supplier to a semi fixed rate with The Energy Consortium (TEC) and prices had fallen.

6.5 Non DC2 Capital expenditure had been relatively high. This was in part catching up on projects that had slipped from prior years. The level of spend against the budget and the amount of slippage was the best that had been achieved in recent years.

NG/Trustees 6.6 General Fund Provision – There was a discussion about the level of the general fund provision. It was agreed that this would be revisited at the November Board of Trustees meeting when the Director of Finance & Corporate Services presented the draft budget for 2011/12.

ACTION

6(b) Financial Review for the period April 2010 – May 2010

- 6.7 Grant in Aid Within Year Cut - in late May the Museum was notified of a reduction of £1.8m (3%) in the original grant in aid allocation for 2010/11 as a consequence of the new Government's proposals to address public sector finances. Of the reduction £0.3m was attributable to a depreciation allocation and the cash reduction was £1.5m. The cash reduction was accommodated by: (a) release of some of the pay award budget; (b) unallocated capital; (c) external funding above budget; and (d) a general fund surplus.
- 6.8 Judicial Review of the Civil Service Compensation Scheme – the outcome of the judicial review had made it difficult for the Museum to budget for redundancies. The previous government had imposed a new less generous scheme having secured agreement from five of the six Civil Service trade unions. The sixth union PCS asked for a judicial review and the High Court found that the new scheme which was to take full effect on 1st April 2011 should not have been brought in without full agreement.
- 6.9 The situation now was that staff made redundant before 15th September 2010 will be made redundant under the old scheme. However, redundancy notices issued to staff that will be made redundant after 15th September 2010 will on legal advice state the redundancy terms will be those payable at the time of the expiry of the 6 month redundancy notice. In November 2009 the Museum had made a redundancy provision of £1.2m when the full number of NHM staff redundancies was not known. The current estimate of the actual cost under the old compensation scheme was £1.5m. If the timetable for redundancies slips and staff were made redundant after 1st April 2011 the Museum will incur monthly salary costs of £180k which had not been budgeted for.

6(c) Restless Planet Update

- 6.10 There had been no movement since the previous report.

7. THE ANNUAL ACCOUNTS 2009/2010 - MANAGEMENT LETTERS, NAO AUDIT COMPLETION REPORT, ISA 260 AND THE STATEMENT ON THE SYSTEM OF INTERNAL CONTROL (PAPER TAC 21/2010)

7(a) The Natural History Museum Annual Report and Accounts

- 7.1 There had been an informal review of the accounts by the Chairman of the Audit & Risk Committee and Mark Richardson (co-opted member) on 22nd June 2010.
- 7.2 The Accounts were currently with DCMS for comment. There were some minor text changes to be made, however, the audit work had been completed. After the approval of the Accounts at the Board of Trustees meeting on 6th July 2010 the Accounts will be sent for ministerial approval. The Director of Finance & Corporate Services was seeking to lay the accounts the week beginning 12th July 2010 subject to the availability of the Comptroller & Auditor General to sign the Accounts. This was well in advance of the parliamentary summer recess on 29th July 2010.
- 7.3 “Going Concern” Assessment – the “Going Concern” assessment covered the first three months of the next financial year. The Museum had been requested to provide DCMS with an indication of how it would seek to manage reductions of both 25% and 30% in its budget over four years. There was, however, no guidance whether this reduction would or should be linear over the four years. The Director was comfortable that the proactive work that had been done to prepare for cuts in 2011/12 meant that a “going concern” assumption would be able to be made once the exercise for DCMS had been completed. .

ACTION

NG/Trustees 7.4 It was agreed that there would be a discussion on the outcome of the DCMS exercise and the “Going Concern” assessment at the Board of Trustees on 6th July 2010. The minutes of the Board meeting were to record the “Going Concern” assessment.

7.5 Statement on Internal Control – this included reference to the loss of the bird skins from the Natural History Museum at Tring.

7(b) NAO Audit Completion Report and ISA 260 Communication of Audit Matters to those charged with Governance

7.6 The PKF Partner presented the NAO Report

7.7 Overall Conclusion – The Comptroller and Auditor General was expected to certify the accounts with an unqualified audit opinion and without modification.

Significant Areas

7.8 The PKF Partner highlighted the following issues.

7.9 Heritage Assets – Financial Reporting Standard (FRS 30) Heritage Assets set out new disclosure requirements for the reporting of Heritage Assets, which apply whether or not they were reported on the balance sheet. This standard applied to accounting periods commencing on or after 1st April 2010 but early adoption was encouraged. As for other institutions the Museum had not adopted FRS 30 early. FRS 30 encouraged the capitalisation on the balance sheet of heritage assets. However, there was no requirement to value assets as it was recognised: (a) this maybe prohibitively expensive; or (b) it may not be possible to obtain a reliable valuation. It was up to the Museum decide how to apply FRS 30 and the amount of information provided. There must be audit evidence to support any disclosures such as the number of items in the collections. Members generally agreed that an internal audit or valuation of 78 million specimens would not be cost effective or practical. The Museum was well placed to meet the new disclosure requirements as there was currently a detailed note on collections management in the Accounts.

NG/Trustees 7.10 It was agreed that the NHM treatment of Heritage Assets under FRS 30 would be discussed, approved and minuted at the November 2010 Audit & Risk Committee.

Audit Findings and Recommendations

7.11 Retention of documentation – documentation to support season ticket loan applications should be retained for 6 years.

7.12 Non-capitalisation of donated assets – assets donated to the Museum’s collections e.g. minerals were not being capitalised in the balance sheet as required by the Charities Statement of Recommended Practice (SORP). There was a risk that: (a) the accounts will not comply with FRS 30 when it comes into force; and (b) the value of donated assets will become material overtime. FRS 30 did not require external valuations. It was noted that NHM curators were the experts in valuing scientific material and carried out valuations for other institutions.

7.13 Multi-year contracts – some contracts spanning three or more years were paid in full at the start of the contract. There was a risk the Museum was not maximising cash flow or that suppliers may become insolvent.

ACTION

- 7.14 Underspend on capital grant – The Museum had not received formal agreement from DCMS to carry forward an underspend of £106k. The Director of Finance & Corporate Services explained that the South Kensington Cultural and Academic Estate (SKCAE) had received a grant of £2.9million from the UK government's Invest to Save budget. The project was lead by the Museum and the partners included the Victoria & Albert Museum, Imperial College, the Science Museum, and the Royal Albert Hall. The grant, was used to purchase equipment to monitor energy efficiency and the underspend related to data analysis and production of the final report. The Director of Finance & Corporate Services said he had now requested formal agreement from DCMS.

Identified Misstatements

- 7.15 The PKF Partner set out the adjustments made to the financial statements and the unadjusted errors arising from the audit. Members endorsed the Director of Finances & Corporate Services reasons for not correcting the misstatements.

7 (c) The Natural History Museum Trading Company Limited and Kingston Smith Management Letter

(a) Trading Company Accounts

- 7.16 The Accounts were approved at a meeting of the Trading Company Directors on 28th June 2010 and were ready to be signed.

(b) Kingston Smith Management Letter

- 7.17 The Kingston Smith Partner presented the Management Letter.

Corrected and uncorrected misstatements

- 7.18 There were no corrected material misstatements. The uncorrected trivial misstatements which totalled £11,100 were approved by the Committee.

Other audit matters of governance interest

- 7.19 There were two instances of minor fraud uncovered internally during the year. Kingston Smith was satisfied, however, that the control systems had been adjusted adequately.

Appendix 1- Major Points

- 7.20 Sales Invoice Control System – manual invoices were raised and sent out by each department, however, copies were not sent to the Finance Department in a timely manner. No action was taken until the year end by Finance to ensure that all invoices were recorded on the system. It was recommended this was done on a monthly basis.

Appendix 2 – Minor Points

- 7.21 Employment Contracts - the Kingston Smith Partner was concerned that the contract for one employee could not be found by the HR Department.

ACTION

7 (d) Special Funds, Benevolent Fund and Cockayne Fund

7.22 The Special Funds Trust and Benevolent Fund accounts were complete and awaiting approval prior to signature by the Chairman of the Board of Trustees.

7 (e) Audit & Risk Committee Approval

7.23 Members:

(a) approved the Special Funds and Benevolent Fund for the Chairman of the Board's action; and

(b) recommended that the consolidated accounts for the Natural History Museum were approved by the Board of Trustees on 6th July 2010 subject to planned amendments.

7.24 The Chairman thanked the Finance team and the external auditors on behalf of the Committee for the successful production of the Accounts.

7.25 Internal Audit and External Audit Risk Exposure – the Chairman noted the government's intention to find savings of 25% in administration costs including consultancy across departments. The Audit & Risk Committee must as a result consider the amount of risk exposure they were prepared to tolerate from less internal and external audit. The Committee were looking for a comparable reduction in the NAO administration costs and audit fee. It was observed that a change in administrative status for Museums may remove the statutory requirement to be audited by the NAO.

7.26 In addition, it was noted that the Cabinet Office had indicated that it was considering relaxing some of the compliance requirements that had been imposed on government departments over the last few years.

8 ACTING HEAD OF RISK & ASSURANCE PROGRESS REPORT TO JULY 2010 (PAPER TAC 22/2010)

8.1 The Acting Head of Risk & Assurance presented her paper.

8.2 The Committee reviewed two full audit reports: (a) the Departmental Audit of Palaeontology; and (b) a summary of the Internet and Internal Network Security Review. The Director had asked that the Network Security Review be included in the papers. The report had been written by the Acting Head of Risk & Assurance at the Director's request. This was to address the concerns of the Committee that the classifications used by the specialist IT auditors in their last report were not synonymous with those used by the Museum.

8.3 Credit Checks New Customers – credit checks on new customers were not always carried out through the Finance Departments as required by the Financial Regulations. This had been raised in previous reports by both the internal and external auditors. Members expressed the view that the risk of insolvency was rising and the Director of Finance & Corporate Services should issue a clear directive to staff which set out the requirement.

NG

ACTION

- 8.4 Risk & Assurance Staffing – the Director reported that following the retirement of the former Head of Risk & Assurance, Jan Day was acting up as Head of the Department. Longer term staffing of this function will be reviewed in the light of: (a) any relevant outputs from the HMT project to review Internal Audit across government; and (b) the Museum’s desire to maintain an effective and detailed regime to review internal controls. However, it was recognised that the size of reduction in government funding will compromise the Museum’s ability to fund the level of internal audit work that had previously been relied upon. The Museum was continuing to operate with contract staff until such time as future resource levels could be established definitively.
- 8.5 The agency auditor who had been working in Risk & Assurance since the beginning of March left on 18th June 2010. In accordance with the Museum’s recruitment freeze the Acting Head of Risk & Assurance had obtained authority to recruit from the HR Director with a view to finding a suitable replacement.

MD/DO 8.6 The Chairman expressed the view of the Committee that the situation was unsatisfactory, however, in the current circumstances unavoidable. It was agreed to return to the issue at the November Audit & Risk Committee.

MD/JD 8.7 Risk & Assurance Plan – the plan was substantial and would be subject to review by the Director and the Acting Head of Risk & Assurance taking into account the available resources.

9. AUDIT AND RISK COMMITTEE ANNUAL REPORT

DO/JD 9.1 The Audit & Risk Committee was required to produce an annual report on the Committee’s own performance and that of the external and internal auditors. It was agreed that Chairman and Acting Head of Risk & Assurance would facilitate the review process and the report would be completed before the November 2010 meeting.

MD 9.2 The Director explained that an external review of the effectiveness of the main Board of Trustees had recently taken place. It was agreed that the next time such a review was undertaken it would be extended to include the Audit & Risk Committee.

10 PRESENTATION BY THE DIRECTOR ON THE MAJOR CORPORATE “RISK FAILURE TO ACHIEVED SUSTAINED GRANT IN AID FUNDING”

10.1 The Director gave his presentation.

10.2 The major corporate risks for 2010/11 had been divided amongst the four members of the new Executive Board. The Director had responsibility for two risks: (a) an incoming new administration introduces a within year cut and prejudices our ability to manage the 2010/11 budget; and (b) failure to achieve sustained grant in aid funding.

10.3 The first risk “an within year cut” had been realised and was being managed by the Museum. The second risk “failure to achieve sustained grant in aid funding” was going to be realised and there was nothing the Museum could do to reduce the likelihood. The question was how well the Museum managed the impact

10.4 The impact and the Museum’s assessment of control were dependent on:

10.5 The DCMS settlement in the Spending Review - this was likely to be no better than average. The Cabinet believed that all departments should make a fair and equitable contribution towards reducing the budget deficit. Jeremy Hunt (Secretary of State for Culture, Olympics, Media and Sport) was unlikely, therefore, to fight for a smaller share of the cuts for DCMS.

ACTION

- 10.6 DCMS's internal deliberations on how to allocate its share of the cuts between the sectors - Jeremy Hunt's decision to cut the Olympics budget as part of the £6.2bn public spending cuts announced by the new government had indicated that no one will be protected.
- 10.7 How well the NHM was perceived within the DCMS - the DCMS peer review 18 months ago gave the NHM a glowing report and the Museum had a good reputation within DCMS. Incoming ministers appreciated that the research undertaken by the Museum on its collections had a public value and significance which was different to other Museums. The NHM, for example, advises: (a) the UK Border Agency on whether imports are illegal under the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES); and (b) the Police on forensics at crime scenes. This work would be lost to government if the NHM scientific research base and collections were damaged by large cuts.
- 10.8 The Museum's preparedness to accommodate cuts - the Museum had been proactive in preparing for cuts in 2011/12.
- 10.9 The Director went onto explain there were a number of confounding factors and he will updating the Board of Trustees on 6th July 2010 .
- 10.10 Review of the Administrative Status of Museums – as stated earlier in the meeting the new government had promised a review of the administrative status of museums. There were 6 or 7 routes forward e.g. making museums “second tier” bodies or independent trusts. However, very few were advantageous to the NHM. The DCMS Museum Directors preferred route of was to create a new status for Museums, however, there appeared to be reticence to consider this. The Director believed that the intention of the new administration was to merge and abolish quangos and take Museums outside of government. The preferred DCMS method to address a change in Museum status was the Public Bodies Reform Bill which will seek to modify or repeal legislation. This may have implications for the legal obligations imposed on the NHM under the British Museum Act 1963.
- 10.11 Independent trust status would take the Museum outside of government. The NHM would be managed as a charity and there were issues about: (a) transferring the obligations under the British Museum Act to an independent trust; and (b) the appointment of Trustees. DCMS Museum Directors did not wish to lose the link with government which was important for the international status of many Museums. The NHM worked in over 70 countries and had formal memoranda of understanding with approximately 30 countries. In addition, the Museum maybe required to leave the Principal Civil Service Scheme and take out insurance to cover risks, for example, to buildings and the collections. The Director was actively lobbying ministers about the negative consequences for Museums.
- 10.12 Most of the Director's effort was concentrated on managing the corporate risk. As Chair of the National Museum Directors' Conference (NMDC), however, he was able to draw on resources outside of the NHM.
- 10.13 DCMS Planning Exercise - DCMS had requested the Museum set out what it would do to deliver administration savings of 33.3% and 50% of current administration spend within an overall 25% and 30% saving. The SORP definition of administration costs that was used in a bench marking exercise of DCMS sponsored bodies had not been adopted for this purpose. The meaning of administration was defined very widely and included everything that supported frontline services.. The submission to DCMS was required by Friday 2nd July 2010 and will include the caveat that it did not have trustees' approval. The approach and the outcome of the exercise will be reported to the Board of Trustees on 6th July 2010 for their approval.
- MD 10.14 The Director gave a preliminary description of the approach the Museum will take to the DCMS exercise.

ACTION

- 10.15 The Director explained that the Executive Board will review and prioritise submissions from Science, Public Engagement and Corporate Services on how they will manage reductions. The areas/functions the Director proposed to protect were: (a) the collections which the Museum had a statutory obligation to maintain; (b) the scientific expertise to make those collections accessible; and (c) income generating trading and fund raising activities. It was noted that certain overheads were fixed and could not be reduced e.g. business rates, heat and lighting.
- 10.16 Admission charges - the maintenance of free admission was written into the new Government's Coalition Agreement. However, the introduction of admission charges would have benefits for the NHM as charging would amongst other things: (a) provide income; (b) reduce visitor numbers which continued to increase; and (c) reduce wear and tear to the infrastructure. Museum funding had not grown in real terms since the introduction of free admission in 2002/2003 and the Director will highlight this in his submission to DCMS.
- 10.17 Efficiency Savings - the Museum would continue with its efforts to find efficiencies through partnerships and shared service provision with other Museums and local institutions. The new government appeared prepared unlike the previous administration to consider projects which had a longer payback period. The strategic review of the library had recommended a more visionary library plan and there was to be a review of the structure for science in 2010. Both these reviews will look for efficiency savings.
- 10.18 Scientific Income – the Museum had a good success rate when applying for EU grants which had been a significant source of funding in recent years. It was noted, however, that grant opportunities from the UK Research Councils and the EU were likely to reduce. It was observed that the Museum should develop its scientific expertise further in those areas where the opportunities for the NHM to win grants were greatest.
- 10.19 Sickness Absence - the Chair of the Board of Trustees observed that the NHM average sickness absence rate appeared to be higher than that in the private sector and that some efficiency could be delivered by addressing this.

11. ANY OTHER BUSINESS

- 11.1 There was no other business.

12. DATE OF THE NEXT MEETING

- 12.1 The next meeting will be held at 10.00 a.m. on Thursday 4th November 2010.

13. CLOSED SESSION WITH THE INTERNAL AND EXTERNAL AUDITORS

- 13.1 There was a confidential discussion.

KEY TO ACTION INITIALS

David Omand - DO

Michael Dixon - MD

Neil Greenwood - NG

Jan Day - JD