

High Speed Two (HS2) Ltd
Audit and Risk Assurance Committee meeting
Wednesday 23 March 2016 at 13:00, Room 502, Sanctuary Buildings, London SW1P 3BP

Present: Neil Masom (Chair) [NM], Roger Mountford [RM]

In attendance: XXXX, XXXX Alistair Kirk [AK], XXXX, XXXX, XXXX (item 2 onwards), XXXX (minutes)

By invitation: XXXX, National Audit Office (item 2.1), XXXX, National Audit Office (items 2.2 and 3.1), XXXX, Genius Methods Ltd (independent Board Effectiveness reviewer)

o. Welcome, Apologies, Declarations of Interest

o.1 Apologies for absence were received from Jo Valentine and Steve Allen.

o.2 There were no changes to the previously declared interests.

1. Assurance: Deep dive reviews

1.1 CPNI Briefing

1.1.1 A closed meeting took place for the discussion of this item, for which no minute was taken.

1.2 Review of RP1 Assurance Report and BL6 Contingency

1.2.1 It was noted the Committee was being asked to endorse the release of the Baseline Six Assurance Report and for ARAC to recommend the findings to DFT in time for a review on 7 April. In addition a project assurance review (PAR) by the IPA was currently in progress which had assigned a provisional 'amber' rating which was due for review by 30 March.

1.2.2 Members observed the presentation was essentially about the affordability of baseline six; completeness of costs and the ability to take the summation.

1.2.3 The Committee discussed the three lines of defence (LOD) assurance reviews which had taken place, and which confirmed those who had undertaken the LOD reviews were comfortable and confident with the findings. It was confirmed Scope and funding were not required for line three LOD.

1.2.4 It was agreed to ensure that the assurance process of the second and third LODs was operating in synchronisation with the Internal Audit Plan 2016/17 leading up to RP2.

Action: Director of Risk and Assurance

1.2.5 It was noted that the LOD assurance of the Schedule had resulted in a 'red' rating which was partly due to the land and property programme. It was agreed to revisit the Top Ten risks to the programme in the Annual Report and Accounts with this in mind.

Action: Director of Finance Operations

- 1.2.6 It was noted that as part of RP1, the Company would need to agree the definition of a 'baseline default' event. A definition would be needed of what was a cost and what was a schedule event.
- 1.2.7 The Committee discussed the scope of BL6 and noted that it took account of approximately 18,000 drawings (included in the hybrid bill submission) for project design and the challenge was to establish if latest drawings had been used. The project design was currently 15% mature and scope may change. Members observed there were many items such as professional fees, incentive payments and Rolling Stock which could not be costed due to uncertainty at this stage.
- 1.2.8 A discussion ensued about why the overall rating had changed from red to amber given the level of certainty as described above. It was noted that the BL6 findings were unlikely to result in a failure to pass through RP1 and the rating should therefore be 'amber/red'. The issue was that the p50 confidence level costs were substantially higher than the strategic prices that were given in the Spending Review.
- 1.2.9 The Chair asked if the SR15 strategic prices would be balanced by RP3. The Director of Risk and Assurance advised that it was expected that there was uncertainty at this stage of the programme and a target was set that was designed to be very stretching: the robustness of the cost estimate was rated amber and was looking reasonably sound.
- 1.2.10 It was agreed the Committee would receive a reworded funding slide. For the final slide, the last bullet point needed to have dates. Action plans for significant findings must be developed and put in place. A hard copy of the full set of slides would be sent to Committee members.

Action: Director of Risk and Assurance

- 1.2.11 The Committee noted that the Company was obliged to be sure that it was comfortable that it would be able to close the funding gap in its presentation of the findings to DFT. Officers confirmed that the headline finding was that the product had moved on significantly, was of better maturity and had more benchmarking and clarity in the detail of components.
- 1.2.12 Members observed that DFT officials were relying on the Company, and Non-Executives were under a duty to decline to approve the report if they were uncomfortable with the level of assurance provided.
- 1.2.13 In conclusion the Committee confirmed it was in agreement that Baseline Six was of sufficient standard of quality and affordability, however the output into using it needed development, and the recommendation was to progress with some concern noted. The Chair noted that he would write a note on behalf of ARAC on the meeting recommendations to the HS2 Ltd Board by the end of the day.

Action: ARAC Chair

2. 2015/16 Year End

2.1 First Draft 2015/16 Financial Statements

Introductory remarks, timescale, approach

- 2.1.1 The Chair set out the timescale for the Annual Report, noting that ARAC would meet to review the final draft on 17 May with a final sign-off meeting on 4 June. At this stage the Chair noted he was keen to have sight of messages coming out of the Chair's and CEO's report. A draft set of accounts would be produced for the Committee to review at its meeting on 22 April; and on 17 May a full set of accounts would be received with an initial update from the NAO.
- 2.1.2 It was noted the document was a set of themes and thoughts with outline versions of the Chair's foreword, CEO's review, Strategic report, Governance statement and Sustainability report produced which would be developed further.

Chair's foreword and CEO review

- 2.1.3 There was a general discussion on the emerging draft and a number of observations were offered:
- 2.1.4 The annual report would attract more comment in several years when quantities of money began to be spent and the programme starts to make a real impact. It was therefore worth envisaging what the scope of the Annual Report was and what the right way of presenting the report was when the sums involved would be exponentially higher.;
- 2.1.5 The document was not as forward looking as it could be. The CEO statement had referred to the size of the engineering project but might discuss other activities and laying plans for operating a major transport service. It might also refer to work in progress on rolling stock and the passenger interface;
- 2.1.6 The establishment of the head office in Birmingham should be mentioned and it should be much plainer that the Company would be based in Birmingham;
- 2.1.7 The report's comment that 'health and safety is our first consideration' could be misleading and could rather be positioned as being 'hugely important'. It was noted that using the Safe at Heart brand, phrasing could be used to reflect that health and safety is one of the core values of the project; and
- 2.1.8 With regard to appointments, outside of new Board members there should be comment on other senior appointments such as Sadie Morgan and Emma Head.
- 2.1.9 Members agreed to provide further comments to the Corporate Finance Director.

Action: ARAC Members

2.2 Annual governance statement / MAS

Annual Governance Statement

- 2.2.1 The Committee reflected on the content of the CEO Report and agreed that the opening of the Birmingham office was a matter for this report whereas the Chair's Report would look at the 'bigger picture' issues. The CEO report should also include comment on the expenditure of the Company's overhead as a means to secure delivery of the hybrid Bill. The wording and content of the CEO report needed to be of the same standard as the Chair's Report.

- 2.2.2 The Committee observed that the Report should include commentary on the delivery of Baseline 6, the first such schedule produced by HS2 Ltd and a fully comprehensive review of the programme.
- 2.2.3 It was noted that the tone needed to be 'preparing to build one of the largest'... and 'laying plans to operate a major transport service'.
- 2.2.4 It was noted the Company begins to capitalise expenditure at second reading, and at third reading it will be able to spend money without recourse to the High Speed Rail Preparation Act.
- 2.2.5 On innovation, this is a huge project and unless we come up with different way of doing it we will struggle to do in traditional way. Innovation, collaboration.
- 2.2.6 Members observed that the commentary could look at the suite of strategies that had been delivered such as the Benefits Strategy. Health and Safety was a key strategic theme of the programme, which led into the development of the scorecard and the deliverables of RP1 and BL6.
- 2.2.7 It was agreed to provide some further text on the supply chain and contracts, particularly engagement sessions with suppliers and potential future suppliers that had taken place.

Action: General Counsel and Company Secretary

- 2.2.8 The Committee observed that the section on the role of the Board should state the Board was accountable for setting the strategy and direction of the organisation, and had delegated certain responsibilities to committees. A comprehensive scheme of delegations and a management structure was in place which flowed down from the Board. It was agreed that the statement should reflect there were parallel structures in that the Accounting Officer was accountable to HM Government and also to the Board. It was agreed that the Review Points as referred to in the text should be defined and should be referred to more explicitly in the commentary.

Action: Company Secretary

- 2.2.9 The following points were raised in relation to other sections of the draft report:
- It was noted that the Risks disclosures were rather dislocated and occurred at several points in the document. Members observed the Network Rail Annual Report was an example of high quality risk reporting and could be used as an example. As previously noted, Land and Property should feature as a 'top ten' risk
 - It was agreed the Report should state that the Company had elected not to remit one of its Board Committees to be responsible for Nominations
 - Sustainability reporting should promote the positive aspects of the project more, for example the reduced carbon emissions that flow from mass transit.
 - The Strategic Report should include commentary around the organisation's view of the key risks and challenges for the coming year
- 2.2.10 It was agreed that a revised draft would be circulated within the next two weeks by correspondence. A further revised draft would then be presented to the next meeting of the Committee on 17 May.

Action: Director of Finance Operations

MAS (Management Assurance Statement)

- 2.2.11 A discussion took place about the Management Assurance Statement which had been submitted earlier in the year.
- 2.2.12 The Committee noted that it had previously discussed the purpose of the MAS and had been advised that the Statement is used to identify areas of risk at an organisational level. Nevertheless it was noted the question remained as to how it should be used to help inform the year-end governance statement.

It was noted that some concerns about security and cyber security had arisen recently, due to a number of laptop computers which had not been returned by employees and contractors who had since left the organisation. The Committee was advised of remedial action being taken including the issuing of legal letters to the individuals identified. Members expressed strong concern over the implications for security and noted it reflected poorly on the culture of the organisation. Officers observed the matter was ultimately linked to the HR starter and leaver process, and certain actions not being documented and closed out when a member of staff or contractor leaves the organisation.

- 2.2.13 It was agreed that the matter would be the subject of an inspection as part of the Internal Audit plan 2016/17 which would be discussed by the Committee on 17 May.

Action: Internal Auditor, HS2 Ltd

Report from DfT Audit Committee Chairs' Meeting

- 2.2.14 It was reported that the group had been briefed on work currently in progress on the development of an assurance framework across the DfT Group. It was noted that there was a lack of wider awareness of this work however notification had been shared with Accounting Officers in February 2016. The review will inform a recommended approach to assurance in the department. It was agreed that the NAO would share a briefing on the work with the Committee Chair.

Action: XXXX, NAO

- 2.2.15 The Committee was advised that the Development Agreement and Framework Document defined the Company's relationship with DfT; however many other documents, such as the assurance framework referred to by DfT were being produced which had a bearing on this relationship.

- 2.2.16 The Committee discussed the matter of the detailed multi-stage approval process for procurement matters and noted this had been raised with DfT. A team at HS2 Ltd was working on mapping the approval and review stages of procurement matters in an effort to bring this work together and it was agreed the findings would be reported to the Committee.

**Action General Counsel /
Assistant Company Secretary**

2.3 NAO progress update and emerging issues / opinion

- 2.3.1 The Committee received an update from the National Audit Office on the year end external audit. It was noted that the inspection was proceeding well and auditors were

encouraged to see progress in relation to matters raised at the last year-end such as the valuation of accruals. It was therefore expected that the opinion would be unqualified.

- 2.3.2 It was reported that some work had been taking place looking at the Capitalisation model and the allocation between resourcing and capital which would form a key accounting policy challenge for the years ahead. It was noted the issue lay at the heart of compliance with SR15.
- 2.3.3 Auditors advised that an issue had been noted around purchase orders and large purchase orders. Improvements had been noted but a further update would be given at year end. On payroll there had also been some improvements with better information available on seconded and permanent staff. There were still some improvements needed around agency staff. However no members of staff had been paid beyond their leaving date.
- 2.3.4 The Committee was advised that the Company was now reaching a level of 95% of suppliers paid within the current month; the level over the whole year is 92%.

2.4 2015/16 Internal Audit progress update and emerging opinion

Progress update

- 2.4.1 The Committee was advised that the 2015/16 internal audit plan had been delivered. Additionally the IT asset management inspection and IT Strategy Report had now been finalised. Management responses for two other reports were expected shortly.
- 2.4.2 The Committee made the following observations in relation to the 2015/16 plan:
- The Planning and Integration review was a two phase review with an advisory piece of work (originally scheduled for last autumn) followed by a review of delivery in September. It was noted the timescales had changed due to the change in the finalisation of the BL6 Assurance Report and RP1, nevertheless this should have been planned, and the Internal Audit service had incurred costs which would need to be flagged to the organisation, and taken into account for the planning of the 2016/17 Internal Audit plan.
 - The Committee observed that for the 2015/16 Internal Audit plan, work in the first quarter of the year had slipped which had meant some work was displaced into the final quarter of the year. The next year's plan should be front end-load so that the final quarter of the year did not fall behind schedule.

**Action: ARAC Chair to discuss
with CFO and Programme
and Strategy Director**

- 2.4.3 With regard to the 2016/17 Plan it was noted the internal audit team had been asked to commence three initial pieces of work including business planning and PSC controls, and the Committee agreed this should proceed, noting that a fuller discussion of the Plan would take place at the next meeting.

Emerging Issues/ Internal Audit Opinion

- 2.4.4 The Committee was advised that the emerging year-end opinion was a 'moderate' and similar to last year, at the lower end of this. The organisation needs to do a quantity of work in terms of maturing and embedding activities. The Committee thanked the Internal Audit for his update and noted this seemed to be a fair reflection of the position at this stage of the Company's maturity. It was noted a robust discussion around the 2016/17 Internal Audit plan would be timetable for the next meeting, to ensure a strong plan was in place for the coming year with which Committee members could be content with.

3. Any Other Urgent Business

3.1 Matters arising

Matter Arising: Update on the External Review by the NAO of Value for Money

- 3.1.1 The Committee received an update from the National Audit Office on an external review of Value for Money. XXXX of the NAO expressed his gratitude to HS2 Ltd and DfT for the co-operation and noted the interviews with key stakeholders, documentation provided and teach-in sessions had been extremely helpful.
- 3.1.2 The Committee was advised of the approximate timetable for the finalisation of the review including the release of draft report, publication of the final report and the likelihood of further external hearings and discussion of the matter.
- 3.1.3 The reviewers had noted the consistency of information received from DfT and HS2 and that there was a real sense of a uniform message of main challenges that the programme faced. An emerging findings meeting with HS2 and DfT would be scheduled for mid-April, and KR would follow up with details.
- 3.1.4 In terms of scope, the Committee was advised this would include programme scope and mapping it onto RP1; organisational readiness and the full programme arch; and benefits realisation such as the relationship between strategic objectives and regeneration.

Other matters arising

- 3.1.5 It was noted the Resource and Recruitment Risk Flightpath should be a standing item on the RemCo agenda.

Action: CFO/HR Director

- 3.1.6 **It was agreed the following matters would be discussed at the next meeting of the Committee: -**

- **Initial priorities for the 16/17 internal audit plan**
- **The CMMI report**
- **Cyber security – the number of documents that are downloaded and stored on laptops.**

Action: Assistant Company Secretary

- 3.1.7 In a related matter, the Committee was advised that the Commercial Panel had received a request for 11 data controllers to comply with new regulations. If this was extrapolated across the organisation more than 100 such individuals would be needed. It was noted this was part of the discussion around work force planning and would need to be picked up on the Business Planning reporting to the HS2 Ltd Board.

3.2 Proposed Review of Approval Process

3.2.1 The Committee was advised that this item was to close an action from a previous meeting and the aims of the proposed review, led by the Company Secretary, were to:

- Bed down the relationship between DFT and HS2 Ltd at RP1 in order to confirm a meaningful delegation and approval structure
- Revisit the foundation documents including the framework agreement
- Cascade these items down into the Company's own standing orders.
- It was reported that the process would conclude with a paper to the HS2 Ltd Board confirming the current situation and a proposal for the cascade of operational delegations and to tidy up ambiguities, for example areas where Standing Orders are currently silent. This would then be cascaded into TORs of the committees.

3.2.2 The Committee noted the update.

3.3 Initial Priorities for the 2016/17 Internal Audit Plan

3.3.1 It was noted this item had been covered in the discussion above including on the theme of laptop losses as part of the MAS discussion.

4. Dates of next meetings: 21 April; 17 May 2016

5. Any Other Business

5.1.1 There was no further business and the meeting closed at approximately 5.00pm.

Signed:

Date: