

ANNUAL REPORT

Directors Report

1. Form of Accounts

The accounts have been prepared in accordance with a direction given by HM Treasury in pursuance of Section 97 of the Government of Wales Act 1998.

2. Background to Health Commission Wales (Specialist Services)

Health Commission Wales (Specialist Services) (HCW) is an Executive Agency of the Welsh Assembly Government. Prior to the NHS restructuring in 2003, specialised health services were either commissioned by individual Health Authorities or were delegated to the Specialised Health Services Commission for Wales (SHSCW). This organisation had been set up as a joint venture of the five Welsh Health Authorities, and operated as a sub-committee of Dyfed Powys Health Authority. On 1 April 2003 Dyfed Powys Health Authority ceased to exist and the responsibility for commissioning all designated specialised health services for the residents of Wales formally transferred to HCW including those specialised services formerly commissioned directly by health authorities. The functions of HCW were established under "The Health Authorities (Transfer of Functions, Staff, Property, Rights and Liabilities and Abolition) (Wales) Order 2003 (SI 2003/813)".

3. Accountability structures

Professor Ken Woodhouse is The Chair of HCW's National Specialised Services Commissioning Board and he reports to the Minister for Health & Social Services. Mr Simon Dean is the Chief Executive and Accounting Officer of HCW, taking over from Stuart Fletcher on 10 January 2006. Simon Dean is directly accountable to Ann Lloyd, the Director NHS Wales. Three directors report to HCW's Chief Executive: Stuart Davies is the Director of Finance, Daniel Phillips is the Director of Corporate Services, and Geoffrey Carroll is the Medical Director. These three directors have been in place throughout 2005-06.

4. Principal Activities

HCW's role is to commission tertiary and other highly specialised services for the population of Wales. HCW also has commissioning responsibility for a range of designated services provided on a national basis including blood and screening services and NHS Direct. HCW also has a role in giving advice to NHS Wales on the commissioning of specialised services.

5. The National Commissioning Advisory Board

The National Commissioning Advisory Board (the Board) meets bi-monthly. The Board advises the Chief Executive of HCW and its key role is to consider and sign off the HCW National Commissioning Strategy and Annual Commissioning Plans. The Board will make recommendations to the Director, Health and Social Care Department and Minister for Health and Social Services, Welsh Assembly Government through the Chief Executive and monitor the implementation of the approved plan. Further information on the Board and its membership can be found in the Statement of Internal Control.

6. Pension liabilities

The accounting policy for the treatment of pension liabilities is explained in Note 1.f. to the Accounts.

7. Disabled Persons

HCW follows the Civil Service Code of Practice on Employment of Disabled People. Its policy is to give full and fair consideration to applications for employment made by disabled persons, having regard to their particular aptitudes and abilities.

8. Employee Consultation

HCW is part of the National Assembly for Wales, which has established Whitley Committees, with employee representatives, to discuss matters of concern. Staff are also consulted over the planning process and regular consultation meetings are held between senior and junior staff.

9. Creditors Payment Policy

HCW follows the principles of the Government's Better Payment Practices Code and is committed to paying all undisputed invoices within 30 days of receipt. For the financial year 2005-06 90 per cent of payments by number met this target. (2004-05: 69 per cent).

It is significant that the volume of invoices paid in 2005-06 increased by 8 per cent by number (8 per cent by value) compared to 2004-05 but without a corresponding increase in administration resources. This therefore represents a significant improvement in payment performance.

11. Auditors

The Accounts have been audited by the Auditor General for Wales in accordance with Section 97 of the Government of Wales Act 1998. No amount has been paid to HCW's auditors for non-audit work.

So far as I am aware, there is no relevant audit information of which the entity's auditors are unaware. I have taken all the steps that ought to have been taken to make myself aware of any relevant audit information and to establish that the entity's auditors are aware of that information.

Management Commentary

Position, development and performance of HCW during the financial year

In the financial year 2004-05 HCW was allocated repayable resource brokerage of £10.2m. Together with this resource brokerage and its funded allocation, HCW identified that it needed to achieve £17.95m savings in 2005-06 to meet the needs identified in its Commissioning Plan.

HCW's financial plan for 2005-06 required full achievement of HCW's savings plan targets of £17.95m, and managing within the approved allocation. However, this plan proved to be only partially successful, with the main areas of unplanned growth in 2005-06 continuing to be:

- Growth in high-cost Individual Patient Commissioning expenditure;
- Problems in repatriation of medium secure patients to Wales due to delayed discharges and prison and high care transfers;
- Child and Adolescent Mental Health (CAMHS) and eating disorder growth especially in the Gwent and North Wales localities;
- Over-performance of a number of English contracts against the instructions of HCW;
- Non-achievement of NHS Direct savings.

Whilst programme budgets increased to £483,434,000, expenditure increased to £491,717,000. This has led to expenditure exceeding funding by £8,283,000 in the financial year. A Strategic Change and Efficiency Plan (SCEP) was developed and agreed with the Director NHS Wales that provides resource cover for this excess expenditure in 2005-06.

At 31 March 2006 HCW also has £2.1 million of contingent liabilities reflecting the difference between the value of work invoiced by English and Welsh Trusts compared to the liability that HCW will accept. The difference has largely arisen as a consequence of the divergent contracting regimes in England and Wales. HCW has specifically requested English Trusts to work within the resources allocated through the service agreement process and not to over-perform. This direction has not been adhered to by a number of English Trusts. HCW will not be paying for over-performance that it did not specifically request.

Going concern basis of accounting

The accounts for HCW have been prepared on the going concern basis. This basis of accounting has been maintained because HCW has agreed a SCEP for 2006-07 with the Director NHS Wales in July 2006. This SCEP is designed to bring HCW within in-year financial balance by 31 March 2008.

Principal risks and uncertainties affecting HCW

In developing the SCEP HCW has reviewed all previously planned savings and investment priorities in order to prepare a revised plan that is deliverable within the policy framework available. The plan is challenging, with £15.5m (rising to £24.5m by 2008-09) of savings required to break even before any new development programme can be undertaken. HCW has reviewed critical investment priorities and identified the need to find new resources totalling £4.659m in 2006-07 rising to £9.313m by 2008-09.

HCW's financial targets in terms of loan cover and repayments are set out below:

	Loan funding / (repayment) £m
2004-05	10.2
2005-06	18.3
2006-07	4.9
2007-08	(5.5)
2008-09	(7.7)
2009-10	(11.7)
2010-11	(8.4)

The SCEP is planned to deliver the required target by a range of initiatives:

- Strategic schemes (£10.4m) that commission and procure services in different ways.
- Efficiency schemes (£8.3m) that deliver services at reduced cost and focus commissioning resources more effectively.
- Disinvestment schemes (£1.5m) that reduce the range and/or volume of services being commissioned against a prioritisation framework.

Whilst the 2006-07 SCEP has been accepted by the Director NHS Wales, significant risks may affect HCW's ability to deliver a balanced outturn position in 2006-07 and subsequent years.

In particular, it will be important to:

- Limit service provision and keep new investment to the absolute minimum.
- Implement a range of service reductions to achieve savings.
- Continue to operate a system in which HCW takes responsibility for making decisions on many hundreds of individual patient referrals each year.
- Manage significant service risk including the volatility of mental health referrals.
- Re-shape the nature of contractual relationships with English providers to focus on those services which cannot be provided in Wales and introduce improved referral management.
- Deliver cash releasing efficiencies against the background of financial pressures on provider organisations.

In order to deliver a balanced position into the future it is necessary to continue to identify where HCW can reduce its level of service commissioning whilst maintaining the provision of safe critical services. It is recognised that delivering the schemes outlined will be highly sensitive but must be considered in the context of their relative importance against the specialist services for which HCW is responsible. To this end, HCW has established a Prioritisation Framework, approved at the June 2006 NCAB meeting, to underpin its decision-making process.

Environmental matters

As part of the 'Greening Operations' from the Welsh Assembly Government, HCW must try to reach a Level 5 Green Dragon Award. All offices under WAG are trying to achieve this award by maximising all recycling and environmental issues. To achieve Level 5 HCW must recycle as much as possible and try to cut back on using excessive electricity, water and consumables. So far, HCW is currently recycling paper, cardboard, wooden pallets, plastic bottles, aluminium cans and waste toners.

Social and community issues

HCW continues to engage fully with health communities and patient networks. HCW involves and consults on substantial changes to health services in accordance with WHC(2004)84 - 'Shaping Health Services Locally'.

Simon Dean
Chief Executive & Accounting Officer
3 August 2006

Remuneration Report

Remuneration Policy

HCW follows the remuneration policy of the National Assembly for Wales. There is an ongoing performance appraisal process and its results are used to inform the annual pay award of the directors and other members of staff. Pay increments are withheld from those who do not perform at a satisfactory level. The performance management process also links to the HCW's strategic planning process ensuring that individual objectives reflect wider team and corporate goals.

The level of pay awarded to each pay grade has regard to the following considerations:

- the need to recruit, retain and motivate suitably able and qualified people to exercise their different responsibilities;
- variations in labour markets and their effects on the recruitment and retention of staff;
- National Assembly policies for improving the public services including the requirement on departments to meet the output targets for the delivery of departmental services;
- the funds available in the National Assembly's expenditure limits;
- the National Assembly's inflation target.

The directors of HCW that are seconded from NHS Trusts are subject to a performance appraisal process in the same way as permanent employees. That appraisal process is then used to inform the NHS Trust's annual pay award. Further details on the remuneration policy of individual NHS Trusts can be found in their published annual accounts.

Service Contracts

Civil service appointments are made in accordance with the Civil Service Commissioners' Recruitment Code, which requires appointment to be on merit on the basis of fair and open competition but also includes the circumstances when appointments may otherwise be made.

Both Mr Simon Dean and Mr Stuart Davies hold appointments which are open-ended until they reach the normal retiring age of 60. The three other directors who have held post during the year have been on fixed-term secondment agreements from various NHS Trusts. Details of the secondments are explained below. Early termination, other than for misconduct, would result in the individual receiving compensation as set out in the Civil Service Compensation Scheme.

Salary

'Salary' includes gross salary; overtime; recruitment and retention allowances; private office allowances and any other allowance to the extent that it is subject to UK taxation. This report is based on payments made by HCW and thus recorded in these accounts. No bonuses or allowances were payable and no element of senior manager remuneration is subject to performance conditions.

Benefits in kind

The monetary value of benefits in kind covers any benefits provided by the employer and treated by the Inland Revenue as a taxable emolument. The salary of the senior staff consists of a gross salary only, except for Dr G Carroll who is paid an allowance of £1,485 (*) (2004-05: £801) for a lease car.

Senior Staff Emoluments (*)

HCW Employees:	Salary (2005-06) £000	Salary (2004-05) £000	Real increase in pension and related lump sum at age 60 £000	Total accrued pension at age 60 at 31/03/06 and related lump sum £000	CETV at 31/03/06 £000	CETV at 01/04/05 £000 Restated	Real increase in CETV as funded by employer £000
Simon Dean Chief Executive (i)	15 - 20	N/A	0 - 2.5	0 - 2.5	4	0	3
Stuart Davies Director of Finance (ii)	65 - 70	60 - 65	0 - 2.5	2.5 - 3.0	43	21	12
Seconded:							
Stuart Fletcher Acting Chief Executive (iii)	75 - 80	95 - 100	0 - 2.5	50 - 52.5	N/A	877	N/A
Dr Geoffrey Carroll Medical Director (iv)	120 - 125	110 - 115	15.0 - 17.5	40 - 42.5	737	454	190
Daniel Phillips Director of Corporate Services (v)	75 - 80	70 - 75	0 - 2.5	20 - 22.5	246	221	14

(*) These figures have been subject to audit.

- (i) Mr Simon Dean's employment at HCW began on 10 January 2006. Therefore, the amounts disclosed above represent those earned in the last three months of the financial year. His contract is subject to a three-month notice period.
- (ii) Mr Stuart Davies has been employed by HCW since 1 April 2003. At 31 March 2006, the NHS pension of Mr Davies was in the process of being transferred into the Civil Service scheme and this was completed after year end. His contract is subject to a three-month notice period.
- (iii) Mr Fletcher was employed by Pembrokeshire and Derwen NHS Trust. He was seconded to HCW and retired on 31 December 2005. The salary shown above is for nine months of 2005-06. The CETV of his accumulated pension is not calculated or disclosed because his retirement has commenced.
- (iv) Dr Carroll is employed by Velindre NHS Trust and is seconded to HCW. Dr Carroll's secondment runs from 1 June 2003 to 31 May 2006 with the option to extend to a maximum of five year. This contract is subject to a three-month notice period.

- (v) Mr Phillips is employed by Cardiff & Vale NHS Trust and his initial secondment ran from 1 April 2004 to 31 March 2006. In the post-year end period Mr Phillips was re-appointed to his role and a new two-year secondment agreed. This contract is subject to a three-month notice period.

Pensions

Pension benefits for all HCW employees are provided through the **Principal Civil Service Pension Scheme (PCSPS)**. All seconded staff remain covered by the provisions of the **NHS Pension Scheme** through their employment with their home organisations.

Staff who have joined HCW with existing membership of the PCSPS may participate in one of three statutory based 'final salary' defined benefit schemes (**classic, premium** and **classic plus**). New entrants to the PCSPS after 1 October 2002 had the choice between membership of **premium** or joining a 'money purchase' stakeholder based arrangement with a significant employer contribution (**partnership pension account**).

(a) Classic Scheme

Benefits accrue at the rate of $1/80^{\text{th}}$ of pensionable salary for each year of service. In addition, a lump sum equivalent to three years pensionable salary is payable on retirement. Members pay contributions of 1.5 per cent of pensionable earnings. On death, pensions are payable to the surviving spouse at a rate of half the member's pension. On death in service, the scheme pays a lump sum benefit of twice pensionable pay and also provides a service enhancement on commuting the spouse's pension. The enhancement depends on length of service and cannot exceed 10 years.

Medical retirement is possible in the event of serious ill health. In this case, pensions are brought into payment immediately without actuarial valuation and with service enhanced as for widow(er) pensions.

(b) Premium Scheme

Benefits accrue at the rate of $1/60^{\text{th}}$ of final pensionable earnings for each year of service. Unlike classic, there is no automatic lump sum, but members may commute some of their pension to provide a lump sum up to a maximum of $3/80^{\text{th}}$ of final pensionable earnings for each years service or 2.25 times pension if greater (the commutation rate is £12 of lump sum for £1 of pension given up). Members pay contributions of 3.5 per cent of pensionable earnings. On death, pensions are payable to the surviving spouse or eligible partner at a rate of $3/80^{\text{th}}$ of the member's pension (before any commutation). On death in service, the scheme pays a lump-sum benefit of 3 times pensionable earnings and also provides a service enhancement on commuting the spouse's pension. The enhancement depends on length of service and cannot exceed 10 years. Medical retirement is possible in the event of serious ill health. In this case, pensions are brought into payment immediately without actuarial reduction. Where the member's ill health is such that it permanently prevents them undertaking any gainful employment, service is enhanced to what they would have accrued to the age of 60.

(c) Classic Plus Scheme

This is essentially a variation of **premium**, but with benefits in respect of service before 1 October 2002 calculated broadly as per **classic**.

Pensions payable under **classic**, **premium** and **classic plus** are increased in line with the Retail Price Index.

(d) Partnership Pension Account

This is a stakeholder type arrangement where the employer pays a basic contribution of between 3 and 12.5 per cent (depending on the age of the member) into a stakeholder pension product. The employee does not have to contribute but where they do make contributions, these will be matched by the employer up to a limit of 3 per cent of pensionable salary (in addition to the employer's basic contribution). Employers also contribute a further 0.8 per cent of pensionable salary to cover the cost of risk benefit cover (death in service and ill health retirement). The member may retire at any time between the ages of 50 and 75 and use the accumulated fund to purchase a pension. The member may choose to take up to 25 per cent of the fund as a lump sum.

No employees have opened partnership pension accounts.

There were no pension contributions prepaid at the balance sheet date.

NHS Pension Scheme

This scheme is an unfunded, defined benefit scheme that covers NHS employees, General Practices and other bodies allowed under the direction of Secretary of State, in England and Wales. The cost of the employer contributions due in respect of the seconded staff has been reimbursed by HCW and is shown in Note 2a. Further information about the scheme and details of the latest actuarial valuation are contained in the NHS Pension Scheme (England and Wales) Resource Account, available on the NHS Pensions Agency website www.nhspa.gov.uk or from the Stationary Office.

Cash Equivalent Transfer Values

A Cash Equivalent Transfer Value (CETV) is the actuarially assessed capitalised value of the pension scheme benefits accrued by a member at a particular point in time. The benefits valued are the member's accrued benefits and any contingent spouse's pension payable from the scheme. A CETV is a payment made by a pension scheme or arrangement to secure pension benefits in another pension scheme or arrangement when the member leaves a scheme and chooses to transfer the benefits accrued in their former scheme. The pension figures shown relate to the benefits that the individual has accrued as a consequence of their total membership of the pension scheme, not just their service in a senior capacity to which disclosure applies. The CETV figures include the value of any pension benefit in another scheme or arrangement which the individual has transferred to the Civil Service pension arrangements and for which the CS Vote has received a transfer payment commensurate with the additional pension liabilities being assumed. They also include any additional pension benefit accrued to the member as a result of their purchasing additional years of pension service in the scheme at their own cost. CETVs are calculated within the guidelines and framework prescribed by the Institute and Faculty of Actuaries.

Please note that the factors used to calculate the CETV were revised on 1 April 2005 on the advice of the Scheme Actuary. The CETV figure for 31 March 2005 has been restated using

the new factors so that it is calculated on the same basis as the CETV figure for 31 March 2006.

Real increase in CETV

This reflects the increase in CETV effectively funded by the employer. It takes account of the increase in accrued pension due to inflation, contributions paid by the employee (including the value of any benefits transferred from another pension scheme or arrangement) and uses common market valuation factors for the start and end of the period.

Simon Dean

Chief Executive & Accounting Officer

3 August 2006

STATEMENT OF ACCOUNTING OFFICER'S RESPONSIBILITIES

Under the Government Resources and Accounts Act 2000 and Section 97 of the Government of Wales Act 1998, the HM Treasury has directed Health Commission Wales to prepare a statement of accounts for each financial year in the form and on the basis set out in the accounts direction. The accounts are prepared on an accrual basis and must give a true and fair view of the Agency's state of affairs at the year end and of its income and expenditure, total recognised gains and losses and cash flows for the financial year.

HM Treasury has designated the Chief Executive of Health Commission Wales as the Accounting Officer for the Agency. The Chief Executive's responsibilities, as Accounting Officer, include the responsibility for the propriety and regularity of the public finances, and for the keeping of proper records and preparing the financial statements. These are set out in the National Assembly for Wales Accounting Officers' Memorandum, issued by the HM Treasury.

In preparing the accounts the Accounting Officer is required to comply with the *Financial Reporting Manual* prepared by HM Treasury, and in particular to:

- observe the accounts direction issued by the HM Treasury, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- make judgements and estimates on a reasonable basis;
- state whether applicable accounting standards, as set out in the *Financial Reporting Manual*, have been followed, and disclose and explain any material departures in the financial statements; and
- prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Agency will continue in operation.

The responsibilities of an Accounting Officer, including responsibility for the propriety and regularity of the public finances for which an Accounting Officer is answerable, for keeping proper records and for safeguarding the Department's assets, are set out in the Accounting Officers' Memorandum issued by HM Treasury and published in *Government Accounting*.

Statement of disclosure of information to auditors

So far as the accounting officer, on behalf of the HCW, is aware, there is no relevant audit information of which the HCW's auditors are unaware, and has taken all the steps that ought to have taken in order to make himself aware of any relevant audit information and to establish that the HCW's auditors are aware of that information.

STATEMENT ON INTERNAL CONTROL

1. Scope of responsibility

As Accounting Officer, I have responsibility for maintaining a sound system of internal control within HCW, which supports the achievement of HCW's policies, aims and objectives. I am also responsible for safeguarding the public funds and assets for which I am responsible.

2. The purpose of the system of internal control

The system of internal control is designed to manage risk to a reasonable level rather than to eliminate all risk of failure to achieve policies, aims and objectives; it can therefore only provide reasonable and not absolute assurance of effectiveness.

The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of HCW policies, aims and objectives, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically.

The system of internal control has been in place in HCW for the year ended 31 March 2006 and up to the date of approval of the annual accounts, and accords with HM Treasury guidance.

3. Capacity to handle risk

As Accounting Officer, I have the responsibility of ensuring that appropriate activities take place within HCW to manage risk. I was appointed and took up post in January 2006 by the Director NHS Wales to whom I am accountable. I obtained assurances from my predecessor that controls were in place and operated effectively in the period prior to my appointment. With my appointment came new protocols for reporting risks to the Health & Social Care Department. This has allowed HCW's internal risk management processes to better inform the decision-making processes of NHS Wales as a whole.

The National Commissioning Advisory Board (the Board) meets bi-monthly. The Board's main role is to make recommendations to the Welsh Assembly Government through me and monitor the implementation of the National Specialised and Tertiary services commissioning plan. In addition to agreeing and monitoring the commissioning plan, the Board also advises me on service risks and on the strategic direction of HCW.

The Chair of the Board was appointed by the Minister for Health & Social Services and is responsible for leading the Board and for ensuring that it functions properly and effectively. In addition to the Chair, the membership of the Board consists of representatives from NHS Trusts and Local Health Boards, the voluntary sector, the Association of Welsh Community Health Councils, The National Public Health Service, Welsh Local Government Association and cancer and cardiac networks.

HCW's Clinical Governance Committee is an external group that peer reviews the clinical governance arrangements within HCW and provides advice to me. The membership includes health professionals from a range of specialised areas across NHS Wales as well as representatives from the Community Health Councils, NHS Wales' regional offices, and the Clinical Governance Support and Development Unit in Welsh Assembly Government. Quarterly meetings of this Committee have been held with HCW commissioners and the Medical Director. This has provided the commissioners with an opportunity to discuss issues

within the services for which they are responsible that relate to clinical governance.

A Clinical Governance Development Plan has been developed in the year and has been agreed by the Board. This Plan sets out strategic goals to ensure HCW has clear processes to drive the improvement in and monitor the quality of all services for which it has commissioning responsibility.

The Audit Group acts in an advisory capacity and provides a forum for discussing both internal and external audit matters and seeks to provide assurance to HCW's Accounting Officer on the operation of internal controls. A review of the terms of reference of the Audit Group in light of HM Treasury guidance was carried out in 2005. The membership of the Audit Group expanded to include the Chairman of the Board, HCW's Accounting Officer and two additional external members. In addition to these members, invitees and observers were drawn from the NAW Finance Department and Internal Audit Service, HCW senior management, and the Wales Audit Office.

The internal audit function for HCW is provided by the NAW Internal Audit Services. Internal Audit Services operates to Government Internal Audit Standards. Its work and annual plans are informed by an analysis of the risks to which HCW is exposed. The Head of Internal Audit has carried out three audits at HCW this year. The results of these audits have been agreed by management and have been considered by the Audit Group. The Audit Group has also received and considered the 2005-06 Annual Report prepared by Internal Audit Services.

4. The risk and control environment

HCW has a number of processes for maintaining and reviewing the effectiveness of the system of internal control. The Directors meet weekly to consider the operational issues and plans of HCW. Reports are discussed and appropriate action agreed for managing identified risks and maintenance of the HCW risk register.

I have a Director of Corporate Services who is responsible for ensuring the corporate governance responsibilities set out in the HCW Framework Document are fully met. In particular, this appointment should ensure that HCW has Accountability and Governance Frameworks with clear operational and performance responsibility to the Director NHS Wales. It is also the responsibility of the Director of Corporate Services to lead on the development of a corporate approach to risk management for HCW.

Further to HM Treasury guidance, management has considered the risks facing the organisation and has an organisation-wide risk register. This risk register is a methodology for identifying and assessing the key risks facing the organisation that may adversely affect the achievement of HCW's objectives. Each risk is allocated an owner who is responsible for managing the risk and determining a control strategy. For each identified risk the controls in operation are documented.

In developing the risk register advice was sought from the NAW Financial Governance and Professionalism Division. The risk register has been made available to all staff and the more significant risks are considered at the Directors' meetings. At the strategic level the identified risks are incorporated into the Commissioning Plan and reported to Health & Social Care Division. Ongoing developments to risk management are considered at the quarterly Risk Group. The Risk Group, formed in 2004, is chaired by the Director of Corporate Services and also includes the HCW Financial Accountant and the Clinical Governance Manager. This

Risk Group also considers management's progress in implementing Internal Audit recommendations.

In 2005-06 risk management has continued to develop. During the year there was a formal review of the Assembly functions that have been delegated to me and these functions have, in turn, been delegated to my Directors. Internal Audit Services carried out an audit and reported on risk management in HCW during 2005-06. The report was a positive one and concluded that "HCW has adopted an open and transparent approach to risk management. The risk management process and associated guidance is made available to staff at all levels and steps have been taken to ensure that the risk management is successfully embedded within the culture of HCW". The report was accepted in full and implementation of the recommendations will continue the steady process of improvement in this area.

5. Review of effectiveness

As Accounting Officer I also have responsibility for the review of the effectiveness of the system of internal control. My review is informed by:

- the work of the internal auditors,
- the executive managers within HCW who have responsibility for the development and maintenance of the internal control framework, and
- comments made by the external auditors in their management letter and other reports.

The result of my review of the effectiveness of the system of internal control has been discussed by the Audit Group, and a plan to ensure continuous improvement of the system is in place.

6. Matters of note

HCW is facing considerable financial risk because of its requirement to deliver a balanced outturn position in 2006-07. A SCEP has been agreed with the Director NHS Wales to provide resource coverage and manage this risk. Further information on the SCEP can be found in the Management Commentary.

There were no other matters of note during the year.

7. Statement of assurance

In light of the above, I am satisfied that a sound system of control has operated within the areas for which I am the Accounting Officer.

Simon Dean
Chief Executive & Accounting Officer
3 August 2006

THE CERTIFICATE AND REPORT OF THE AUDITOR GENERAL FOR WALES TO THE MEMBERS OF THE NATIONAL ASSEMBLY FOR WALES

I certify that I have audited the financial statements of Health Commission Wales (Specialist Services) for the year ended 31 March 2006 under Section 97(5) of the Government of Wales Act 1998. These comprise the Operating Cost Statement, the Balance Sheet, the Cashflow Statement and the related notes. These financial statements have been prepared under the accounting policies set out within them.

Respective responsibilities of the Accounting Officer and auditor

The Accounting Officer is responsible for preparing the Annual Report and the financial statements in accordance with Section 97(5) of the Government of Wales Act 1998 and HM Treasury directions made thereunder and for ensuring the regularity of financial transactions. These responsibilities are set out in the Statement of Accounting Officer's Responsibilities.

My responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements, and with International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with HM Treasury directions issued under the Government of Wales Act 1998. I also report whether in all material respects the expenditure and income have been applied to the purposes intended by the National Assembly for Wales and the financial transactions conform to the authorities which govern them. I also report to you if, in my opinion, the Annual Report is not consistent with the financial statements, if Health Commission Wales (Specialist Services) has not kept proper accounting records, if I have not received all the information and explanations I require for my audit, or if information specified by HM Treasury regarding remuneration and other transactions is not disclosed.

I review whether the statement on pages 17 to 28 reflects Health Commission Wales (Specialist Services)'s compliance with HM Treasury's guidance on the Statement on Internal Control, and I report if it does not. I am not required to consider whether the Accounting Officer's statements on internal control cover all risks and controls, or to form an opinion on the effectiveness of Health Commission Wales (Specialist Services)'s corporate governance procedures or its risk and control procedures.

I read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. This other information comprises only the Directors' Report, the Management Commentary and the unaudited part of the Remuneration Report. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the financial statements. My responsibilities do not extend to any other information.

Basis of audit opinion

I conducted my audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. My audit includes examination, on a test basis, of evidence relevant to the amounts, disclosures and regularity of financial transactions included in the financial statements and the part of the Remuneration Report to be audited.

It also includes an assessment of the significant estimates and judgments made by the Accounting Officer in the preparation of the financial statements, and of whether the accounting policies are most appropriate to HCW's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements and the part of the Remuneration Report to be audited are free from material misstatement, whether caused by fraud or error and that in all material respects the expenditure and income have been applied to the purposes intended by the National Assembly for Wales and the financial transactions conform to the authorities which govern them. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Remuneration Report to be audited.

Opinions

In my opinion:

- the financial statements give a true and fair view, in accordance with the Government of Wales Act 1998 and directions made thereunder by HM Treasury, of the state of Health Commission Wales (Specialist Services)'s affairs as at 31 March 2006 and the net expenditure and cashflows for the year then ended;
- the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with HM Treasury directions issued under the Government of Wales Act 1998; and
- in all material respects the expenditure and income have been applied to the purposes intended by the National Assembly for Wales and the financial transactions conform to the authorities which govern them.

I have no observations to make on these financial statements.

Jeremy Colman
Auditor General for Wales
14 August 2006

Wales Audit Office
2-4 Park Grove
Cardiff
CF10 3PA

OPERATING COST STATEMENT FOR YEAR ENDED 31 MARCH 2006

		Year Ended 31 March 2006		Year Ended 31 March 2005	
	<i>Note</i>	£000	£000	£000	£000
EXPENDITURE					
Programme Expenditure	3	(491,717)		(443,268)	
Administration Expenditure:					
Staff	2	(1,668)		(1,450)	
Other administration	4	<u>(150)</u>		<u>(295)</u>	
Total Expenditure			<u>(493,535)</u>		<u>(445,013)</u>
NET COST OF ACTIVITIES			<u>(493,535)</u>		<u>(445,013)</u>
NET EXPENDITURE FOR THE YEAR			<u>(493,535)</u>		<u>(445,013)</u>

The movement on the General Fund is shown at Note 10

All activities are continuing. There are no recognised gains or losses during the year.

The notes on pages 20 to 28 form part of these accounts

BALANCE SHEET AS AT 31 MARCH 2006

		31 March 2006		31 March 2005	
	Note	£000	£000	£000	£000
CURRENT ASSETS					
Debtors	7	1,937		2,174	
Cash at bank and in hand	8	311		2,131	
		<u>2,248</u>		<u>4,305</u>	
CREDITORS					
Amounts falling due within one year	9	<u>(21,874)</u>		<u>(11,914)</u>	
NET CURRENT LIABILITES			<u>(19,626)</u>		<u>(7,609)</u>
TOTAL ASSETS LESS CURRENT LIABILITIES			(19,626)		(7,609)
CREDITORS					
Amounts falling due after more than one year	9		(166)		(166)
NET LIABILITIES			<u>(19,792)</u>		<u>(7,775)</u>
FINANCED BY TAXPAYERS EQUITY					
General fund	10		(19,792)		(7,775)
TOTAL GOVERNMENT FUNDS			<u>(19,792)</u>		<u>(7,775)</u>

Simon Dean
 Chief Executive & Accounting Officer
 3 August 2006

The notes on pages 20 to 28 form part of these accounts

**CASH FLOW STATEMENT
for the year ended 31 March 2006**

	<i>Note</i>	2005-06 £000	2004-05 £000
Net cash outflow from operating activities	12a	(483,517)	(447,910)
Financing from the National Assembly for Wales	10	481,697	448,287
Increase/ (decrease) in cash in the period	12b	<u>(1,820)</u>	<u>377</u>

The notes on pages 20 to 28 form part of these accounts

NOTES TO THE ACCOUNTS

1. Accounting Policies

a. Basis of Accounting

The financial statements have been prepared in accordance with the Accounts Direction issued by HM Treasury on 29 June 2005 pursuant to Section 97 of the Government of Wales Act 1998.

The Accounts follow the requirements of the Financial Reporting Manual issued by HM Treasury and are based on the accruals concept of accounting and the historical cost convention.

Subject only to compliance with the requirements set out in the Accounts Direction, the Accounts also:

- i. Comply with the accounting and disclosure requirements of the Companies Act 1985 in so far as they are consistent with the status of an Agency of the National Assembly for Wales; and
- ii. Comply with accounting standards issued or adopted by the Accounting Standards Board except to the extent that they are advised inapplicable by HM Treasury.

b. Funding

The main source of funding for HCW is from the National Assembly for Wales and is credited to the General Fund on receipt.

Liabilities at the balance sheet date will be partly discharged by funding provided in later financial years as part of the Strategic Change and Efficiency Plan (SCEP) agreed with the Welsh Assembly Government (see Management Commentary).

c. Expenditure

The expenditure recognised in the accounts represents the cost of treatments carried out in the year. In common with NHS commissioners HCW has in place service level agreements covering the provision of health services with all main providers. The majority of HCW's expenditure is incurred under cost and volume Service Level Agreements (SLAs). These SLAs, agreed on a rolling one-year basis are not legally binding. Contracts with NHS organisations on an individual patient commissioning (IPC) basis are also not legally binding. A small proportion of HCW's expenditure is incurred under legally binding contracts with the new Foundation Trusts in England or private sector providers of primarily secure mental health services.

d. Value Added Tax (VAT)

HCW is covered by the VAT registration of the National Assembly for Wales. HCW recovers VAT on its business activities and on certain contracted out services, as agreed by HM

Treasury. Expenditure shown in the Income and Expenditure Account includes VAT except where VAT is recoverable in conjunction with the business activity or contracted-out service.

e. Leases

Rentals payable under operating leases are charged on a straight line basis over the terms of the lease.

f. Pension Costs

Past and present employees are covered by the provisions of the Civil Service Pension Scheme, which is described at Note 2. The defined benefit elements of the schemes are unfunded and are non-contributory except in respect of dependants' benefits. HCW recognises the expected cost of these elements on a systematic and rational basis over the period during which it benefits from employees' services by payment to the Principal Civil Service Pension Schemes (PCSPS) of amounts calculated on an accruing basis. Liability for payment of future benefits is a charge on the PCSPS. In respect of the defined contribution elements of the schemes, HCW recognises the contributions payable for the year; these amounts are charged to the Income and Expenditure account in the year of payment.

g. Notional Costs

A notional cost has been included to cover certain common services and support functions, such as finance, personnel, accommodation and other office services, provided to HCW by the National Assembly for Wales free of charge.

A notional interest has been calculated at the appropriate government lending rate (3.5%) on the average value of net current liabilities in the year.

h. Capitalisation of equipment

The minimum level for capitalisation of individual assets is £5,000. All other equipment purchases of individually lower value are treated as other administrative expenditure items in the accounts.

2. Staff numbers and costs

a) Staff Costs

				2005-06	2004-05
	HCW employees	Secondees	Agency	Total	Total
	£000	£000	£000	£000	£000
Wages & Salaries	702	592	236	1,530	1,268
Social Security Costs	59	58	-	117	104
Other Pension Costs	144	83	-	227	168
	905	733	236	1,874	1,540
Funding from NLIAH for referral centre salaries	(57)	(32)	(11)	(100)	-
Funding for seconded out staff	(106)			(106)	(90)
Total	742	701	225	1,668	1,450

b) Staff Numbers

The average number of whole-time equivalent persons (including Senior Staff) employed during the year was:

	2005-06	2004-05
HCW employees	18	15
Secondees	10	11
Agency	9	7
Total	37	33

c) Pension Schemes

Pension benefits for all HCW employees are provided through the **Principal Civil Service Pension Scheme (PCSPS)**. All seconded staff remain covered by the provisions of the **NHS Pension Scheme** through their employment with their home organisations.

Principal Civil Service Pension Scheme (PCSPS)

This is an unfunded multi-employer defined benefit scheme but HCW is unable to identify its share of the underlying assets and liabilities and therefore falls within the multi-employer exemption provided by FRS17, Retirement Benefits, and accounts for its contributions to the scheme as though this was a defined contribution scheme. A full actuarial valuation was carried out at 31 March 2003. Details can be found in the resource accounts of the Cabinet Office: Civil Superannuation (www.civilservice-pensions.gov.uk).

For 2005-06, employers' contributions of £143,670 (2004-05: £94,713) were payable to the PCSPS at one of four rates in the range 16.2 to 24.6 per cent of pensionable pay, based on salary bands. The Scheme's Actuary reviews employer contributions every four years following a full scheme valuation. From 2006-07, the salary bands will be revised and the rates will range between 17.1% and 25.5%. The contribution rates are set to meet the cost of the benefits accruing during 2005-06 to be paid when the member retires, and not the benefits paid during this period to existing pensioners

NHS Pension Scheme

This scheme is an unfunded, defined benefit scheme that covers NHS employees, General Practices and other bodies allowed under the direction of Secretary of State, in England and Wales. The cost of the employer contributions due in respect of the seconded staff has been reimbursed by HCW and is shown in Note 2a. Further information about the scheme and details of the latest actuarial valuation are contained in the NHS Pension Scheme (England and Wales) Resource Account, available on the NHS Pensions Agency website www.nhspa.gov.uk or from the Stationary Office.

d) Chair of National Commissioning Advisory Board

Professor Ken Woodhouse is Chairman of the National Commissioning Advisory Board. HCW paid his employer University of Wales College of Medicine £8,936 during the year for his services. No expenses were paid in respect of 2005-06.

Members of the National Commissioning Advisory Board do not receive any emoluments and were not reimbursed any expenses in respect of 2005-06.

3. Programme Expenditure

The note below gives an analysis of programme expenditure by Provider for the year.

	2005-06	2004-05
	£000	£000
NHS:		
Cardiff & Vale NHS Trust	130,838	120,188
Welsh Ambulance Services NHS Trust	81,244	65,069
Swansea NHS Trust	80,062	72,768
Velindre NHS Trust	49,887	43,192
North East Wales NHS Trust	8,924	8,604
Bro Morgannwg NHS Trust	12,256	9,743
Other Welsh NHS Trusts	16,636	15,602
Other NHS Organisations	76,124	74,940
Non-NHS:		
Llanarth Court	9,499	9,744
Other providers of health care	26,247	23,418
	491,717	443,268

During 2005-06 additional specialist services were identified and commissioning responsibility and resource limit transferred to HCW from Local Health Boards. In 2005-06 an

additional resource allocation of £980,000 was provided to HCW to pay for these newly transferred services. In addition to the inflationary uplifts, service growth and newly transferred services, £17.7 million was allocated to HCW to fund Agenda for Change expenditure in Welsh NHS Trusts.

4. Administration expenditure

	2005-06	2004-05
	£000	£000
Central administration	54	65
Information Technology	120	-
Travel, subsistence and hospitality	72	103
Review Panel Remuneration	37	51
Auditor's remuneration	45	-
Other	1	2
	<hr/> 329	<hr/> 221
Non-cash items:		
- cost of capital credit	(483)	(331)
- notional charge for National Assembly for Wales services	304	350
- auditor's remuneration	-	55
	<hr/> (179)	<hr/> 74
	<hr/> 150	<hr/> 295

5. Movements in working capital other than cash

	2005-06	2004-05
	£000	£000
(Increase) / decrease in debtors	237	(1,075)
Increase / (decrease) in creditors falling due within one year	9,960	(1,896)
	<hr/> 10,197	<hr/> (2,971)

6. Hire and operating lease rentals

	2005-06	2004-05
	£000	£000
Hire of plant and machinery	-	3
	<hr/> -	<hr/> 3

Operating lease rental charges were payable by the National Assembly for Wales in 2005-06.

Commitments under non-cancellable operating leases:

	£000	£000
Within 1 year	3	3
Between 1 and 5 years	7	10
After 5 years	-	-
	<u>10</u>	<u>13</u>

7. Debtors

	31 March 2006 £000	31 March 2005 £000
Amounts falling due within one year:		
Trade debtors:		
Welsh NHS Trusts	900	1,076
Welsh Local Health Boards	29	319
English NHS Trusts	988	714
Non NHS		
Other Central Government bodies	-	52
Other providers of healthcare	16	-
VAT Reclaimable	-	11
Prepayments and accrued income	4	2
	<u>1,937</u>	<u>2,174</u>

8. Cash at bank and in hand

	31 March 2006 £000	31 March 2005 £000
Balance at 1 April	2,131	1,754
Net cash inflow/(outflow)	(1,820)	377
Balance at 31 March	<u>311</u>	<u>2,131</u>

The Office of HM Paymaster General (OPG) provides a current account banking service. The following balances were held at 31 March:

	31 March 2006 £000	31 March 2005 £000
Balances at OPG	285	2,129
Commercial Banks and cash	26	2
	<u>311</u>	<u>2,131</u>

9. Creditors

	31 March 2006 £000	31 March 2005 £000
Amounts falling due within one year:		
Trade creditors:		
Welsh NHS Trusts	8,909	3,352
Welsh Local Health Boards	142	486
English NHS Trusts	7,849	5,404
English Primary Care Trusts	179	13
Non NHS	4,469	2,600
Other creditors and deferred income	326	59
	21,874	11,914
Amounts falling due after more than one year:		
Trade creditors:		
Non NHS	166	166
	166	166

10. General Fund

	2005-06 £000	2004-05 £000
Funding	481,697	448,287
Net expenditure for the year	(493,535)	(445,013)
Notional cost adjustments:		
- cost of capital	(483)	(331)
- notional charge for National Assembly for Wales services	304	350
- auditors remuneration	-	55
Net increase / (decrease) in general fund	(12,017)	3,348
General fund at 1 April 2005	(7,775)	(11,123)
General fund at 31 March 2006	(19,792)	(7,775)

11. Reconciliation of movements in government funds

	2005-06 £000	2004-05 £000
Movement on General Fund for the year	(12,017)	3,348
Government funds at 1 April 2005	(7,775)	(11,123)
Government funds at 31 March 2006	(19,792)	(7,775)

12. Notes to the Consolidated Cash Flow Statement

12(a). Reconciliation of net cost of operating activities to net cash outflow from operating activities

Net cost of operating activities for the year		(493,535)	(445,013)
Adjustments for non-cash transactions	4	(179)	74
Adjustments for movements in working capital other than Cash	5	10,197	(2,971)
Net cash outflow from operating activities		(483,517)	(447,910)

12(b). Reconciliation of Net Cash flow to movement in net funds

Increase/(decrease) in cash		(1,820)	377
Net funds at 1 April 2005		2,131	1,754
Net funds at 31 March 2006		311	2,131

13. Commitments

There were no capital commitments at 31 March 2006

Other commitments relating to Named Patient Service Agreements amounted to £1,429,789 at 31 March 2006. This represents the level of treatments agreed during 2005-06 but not carried out prior to 1 April 2006.

14. Contingent liabilities

HCW has £2.1 million of contingent liabilities reflecting the difference between the value of work invoiced by English and Welsh Trusts compared to the liability that HCW will accept. The difference has largely arisen as a consequence of the divergent contracting regimes in England and Wales. HCW has specifically requested English Trusts to work within the resources allocated through the service agreement process and not to over-perform. This direction has not been adhered to by a number of English Trusts. HCW will not be paying for over-performance that it did not specifically request.

15. Financial Instruments

FRS 13, *Derivatives and Other Financial Instruments*, requires disclosure of the role which financial instruments have had during the period in creating or changing the risks an entity faces in undertaking its activities. Because of the non-trading nature of its activities and the way in which Agencies are financed, HCW is not exposed to the degree of financial risk faced by business entities. Moreover, financial instruments play a much more limited role in creating or changing risk than would be typical of the listed companies to which FRS 13 mainly applies. HCW has very limited powers to borrow or invest surplus funds and financial assets and liabilities are generated by day-to-day operational activities and are not held to change the risks facing HCW in undertaking its activities.

- Liquidity Risk - HCW is financed by the National Assembly for Wales and is therefore not exposed to liquidity risks.

- Interest Rate Risk and Foreign Currency Risk - HCW's financial assets and liabilities are not exposed to interest rate or foreign currency risks.
- Fair Values - There is no difference between the book values of HCW's financial assets and liabilities as at 31 March 2006.

16. Related Party Transactions

HCW is an Executive Agency of the National Assembly for Wales which is therefore regarded as a related party. Other related parties are all Local Health Boards and NHS Trusts in Wales.

During the year HCW had various material transactions with the National Assembly for Wales. A number of HCW senior staff held senior management positions in organisations that HCW had transactions with during 2005-06.

	Organisation	Programme Expenditure £000
Senior staff:		
Stuart Fletcher (retired – 31 December 2005)	Pembrokeshire and Derwen NHS Trust	2
Geoffrey Carroll	Velindre NHS Trust	49,887
Daniel Phillips	Cardiff & Vale NHS Trust	130,838

In addition to this Programme Expenditure, secondees' salaries are reported within Note 2c.

Chairman of the National Commissioning Advisory Board:

Ken Woodhouse	Cardiff University	131
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17. Post Balance Sheet Events

Other than the agreement of HCW's SCEP in July 2006, there have been no events since the end of the financial year which would affect the understanding of the accounts.